

THE INDONESIAN QUARTERLY

Current Event

The Relevance of the Concept of Joint Development
to Maritime Disputes in the South China Sea

Articles

International Cronysm -- the Role of the International Monetary Fund
and the World Bank

Indonesia and the Military at the Crossroads

ASEAN and the ASEAN Regional Forum:
Should "The Driver" Be Replaced?

Civil Society and Development: The Missing Link

Bank Recapitalization Programme:
Measure Toward Economic Recovery



The Quarterly

The Indonesian Quarterly is a journal of policy oriented studies published by the Centre for Strategic and International Studies (CSIS), Jalan Tanah Abang III/23-27, Jakarta 10160. It is a medium for research findings, evaluations and views of scholars, statesmen and thinkers on the Indonesian situation and its problems. It is also a medium for Indonesian views on regional and global problems. The opinions expressed in *The Indonesian Quarterly* are those of their authors and do not necessarily reflect the opinion of the CSIS.

The Logo



To better represent the underlying ideas that gave birth to the CSIS in 1971 the Centre uses as of 1989 the logo that figures on the front cover of this journal. The original, in bronze, designed by G. Sidharta, it consists of a disc with an engraving that depicts the globe which serves as a background to a naked man with an open book laid on a cloth over his lap, his left hand pointing into the book, his right hand raised upwards. Altogether it symbolises the Centre's nature as an institution where people think, learn and communicate their knowledge to whoever are interested, to share it with them, mankind the world over being their concern and the globe their horizon. The nakedness symbolises the open-mindedness, the absence of prejudice, in the attitude of the scholars who work with the Centre, just as it is with scholars everywhere. The inscription reads "*Nalar Ajar Terusan Budi*", which in the Javanese language essentially means that to think and to share knowledge are only the natural consequence of an enlightened mind. It is a *surya sengkala*, that is *chandra sengkala*, a Javanese traditional way to symbolise a memorable year in the lunar calendar, adapted to the solar calendar system. It consists in using words that express the perceived meaning of the commemorated year while marking the year at the same time, each word having a numerical value. Thus, the inscription, in reverse order, represents the year the CSIS was established: 1971.

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Current Event

The Relevance of the Concept of Joint Development to Maritime Disputes in the South China Sea*

Hasjim Djalal

JOINT development concept is a mechanism to achieve a provisional measure pending the solution of a maritime boundary dispute. It is designed for mutual benefit between or among the parties concerned. The problems of maritime boundary could arise either from disagreement with regard to ownership over islands or land territory, or with regard to the delimitation of maritime jurisdictions between opposite or adjacent states.

The United Nations Convention on the Law of the Sea (UNCLOS) 1982 provided possibilities for this provisional measure in Article 74 on Exclusive Economic Zone (EEZ) and in Article 83 on Continental Shelf. The Convention established a number of rules regarding this matter such as:

a. The delimitation of EEZ and continental shelf boundaries between opposite or

adjacent states "shall be effected by agreement" between the parties; thus, not by unilateral assertion or legislation. This implies the need for dialogue and negotiation, not the use of force or threat of force;

- b. The agreement should be reached "within a reasonable time". There is no definition of a "reasonable time". Some delimitation negotiation has lasted for years. It seems that the parties concerned would have to agree with regard to the definition of the "reasonable time" in a particular case;
- c. If within the "reasonable time" an agreement could not be achieved, the parties concerned must resort to dispute settlement mechanism under UNCLOS, including third party mechanism, either in the form of mediation, good offices, arbitration, or even judicial settlement through the International Court of Justice (ICJ) in the Hague or International Tribunal for the Law of the Sea (ITLOS) in Hamburg;

* A Paper presented at the 13th Asia Pacific Roundtable on "Confidence Building and Conflict Reduction", held in Kuala Lumpur, Malaysia, 30 May - 2 June 1999.

- d. Pending the agreement, the states concerned, during the transitional period, shall make every effort to enter into "provisional arrangements of practical nature" in a spirit of understanding and co-operation. The provisional arrangements include the possibility of applying the joint development or joint co-operation concept;
- e. During the transitional period, the parties concerned shall not take measures that may jeopardize or hamper the reaching of the final agreement of the delimitation. The parties concerned are therefore required to exercise self restraint;
- f. Such agreement on provisional basis, including joint development or joint co-operation, shall not prejudice the territorial or jurisdictional claims of each party and the final delimitation between them.

Legally speaking, all states around the South China Sea, except perhaps Taiwan (Chinese Taipei), which are involved in the multiple claims area in the South China Sea around the Spratly Islands are bound by these rules, because they have ratified the UNCLOS 1982, namely Vietnam, Malaysia, Brunei Darussalam, the Philippines and China. Taiwan or Chinese Taipei on itself is not a party to UNCLOS 1982 because it could not sign or ratify or accede to the Convention on its own, and therefore may argue that it is not bound by it, although it should be at least guided by it. Indonesia is a party to UNCLOS 1982 but is not directly involved in the multiple claims area, although it might be affected in the delimitation process, depending on how the respective claimants are pursuing and developing their argument.

In South East Asian waters there have been a number of examples of the joint development concept such as in Timor Sea between Indonesia and Australia. The two countries have negotiated for a number of years with regard to the continental shelf boundary delimitation between them in certain part of the Timor Sea, but were not able to achieve an agreement, particularly due to the disagreement with regard to the legal implication of the geophysical and geomorphological nature of the seabed area in that sea. The difficulty was therefore not territorial in nature, but technical, because Australia did recognize *de facto* and *de jure* Indonesian sovereignty over East Timor.

The two countries, after some years of negotiation, finally agreed to apply the concept of joint development in the disputed area (Timor Gap Agreement). *First*, they have to agree on the zone to be subjected to the joint development concept (JDZ). It covers an area which is claimed by both sides. Then they agreed on the subjects that could be jointly developed, namely oil and gas. They agreed that the parties to the joint development agreement are the two governments and the agreement to that effect was formulated and approved by the two countries in accordance with their respective constitutional mechanisms. Then a mechanism for such co-operation was established, namely through a joint Authority and a ministerial council to administer the zone. The agreement further divided the zone into three areas and regulated in detail the division of revenue of the three areas. It also stipulated civil and criminal jurisdiction in the zone. The agreement is valid

for 50 years and does not prejudice the final solution of maritime boundaries between the two countries in the future. As it turned out, Indonesia and Australia did later negotiate and agreed on the delimitation of EEZ boundaries in the area which is not the same with the boundaries of the joint development zone. Fisheries exploitation is not included in the JDZ agreement but subject to the EEZ delimitation and to the understanding on the protection of Indonesian traditional fishing rights in clearly defined area falling within the Australian EEZ.

There have been other joint development agreements in the South China Sea, namely between Thailand and Malaysia, and between Malaysia and Vietnam in the Gulf of Siam (Gulf of Thailand). The nature of these agreements is similar to the Timor Gap agreements. There is no territorial disputes in these cases. The problems are overlapping jurisdictional claims over the EEZ and the continental shelf between them. Like the Timor Gap agreement, the areas of the joint development are clearly demarcated, the subjects for the joint development are clearly defined, the mechanism for such joint development is also properly agreed upon and the parties are also well agreed. But, unlike the Timor Gap agreement, the joint developments in the Gulf of Siam are only for 40 years. The agreements also do not prejudice the final delimitation of the maritime boundaries between the countries concerned in the area.

The idea to apply joint development concept to the disputed area in the South China Sea is not new. It was already suggested by the then Chinese Prime Min-

ister Li Peng in his speech in Singapore in 1990 and has since been obediently repeated by Chinese personalities. The former Chinese Prime Minister stated that China is willing to shelve its territorial claims in the South China Sea in favor of joint development between the parties for mutual benefit. But, as it turned out later, it seems that what China has in mind was not properly understood by others. It seems that China would like to jointly develop bilaterally, an area in the South China Sea claimed by others. It is not at all clear whether China would also be willing to consider multilateral joint development for an area or areas which are multilaterally claimed by several states in "multiple claimed area" around the Spratly Island groups. It has been known that China has proposed to Vietnam to jointly develop the area off South Vietnam which China has given concession to Crestone Oil Company, and an area off the coast of North Vietnam which Vietnam has also given concession to other contractor. Vietnam has rejected both of these offers on the ground that the two areas concerned are close to Vietnamese coast lines and regarded by Vietnam as within the limit of its continental shelf.

The Workshop on Managing Potential Conflict in the South China Sea which has been organized since 1990, has also since the very beginning recognized the need for the joint development or joint co-operation in the disputed area. In its second meeting in Bandung in 1991, the Workshop in its statement issued at the end of the meeting stated that "in areas where conflicting territorial claims exist,

the relevant states may consider the possibility of undertaking co-operation for mutual benefit, including exchanges of information and joint development". This issue was taken up again in the Third Workshop in Yogyakarta in July 1992. In its Yogyakarta statement, the Workshop stated among others that "on resources assessment, participant supported the idea of living and non living resources assessment, as well as investigating direction for further co-operation that did not impact on or attempt to prejudice questions of territorial sovereignty", and reaffirmed the agreement achieved in the previous year in Bandung, as well as the need for "co-operation in the disputed area without prejudice to territorial claims and in the common interest of the countries concerned". As a concrete step to achieve co-operation, the Workshop further agreed to establish two working groups to prepare and, after approval by governments, organize joint activities on the following topics: Resources Assessment and Ways of Development; and Marine Scientific Research.

With regard to the resources assessment and ways of development, the workshop agreed "to conduct technical meetings to co-operate on the assessments of living and non living resources, and on option for the development of ground rules, including the possibility of joint development, in an area to be defined".

The Technical Working Group on Resources Assessment and Ways of Development (TWG-RAWD) met in Jakarta in July 1993 and discussed the topics in 4 areas, namely on fisheries, hard minerals, hydro carbon, and other resources. With

regard to **fisheries** the TWG agreed that "co-operative fisheries stock assessment activities should be undertaken with the objective of estimating the abundance and distribution of fish stocks which maybe harvested along the principles of conservation, proper management, maximum sustainable yield, and optimum utilization of fisheries stock". It is also decided that the "fisheries stock assessment activities should cover the whole area of the South China Sea". The TWG further elaborated the detail of the activities, including the role of the fisheries experts in the region, the scope of the activities, the possible methods that might be employed, as well as the legal basis for such activities, particularly Article 123 of UNCLOS. Respective focal points in the region would be indicated and Thailand would co-ordinate the activities. Thailand has prepared a program for this purpose and the Thai proposal has been discussed twice by the Workshop. The Workshop is still studying the Thai proposal.

With regard to the **hard minerals**, it was agreed to undertake co-operation to study seabed resources in the South China Sea area utilising, where possible, the available data in the possession of CCOP, SOPAC, ESCAP, and other regional and international sources. It was further agreed that "such study should start with the exchanging and analysing of available geological and geophysical data that exist in their own country, and as far as possible, accompanied by the detailed assessment of the potential mineral resources that may be found in the South China Sea area". The objective was "to produce a compiled data map on the po-

tential mineral resources in the South China Sea that could be used to further promote co-operative efforts in the South China Sea area". Again it was agreed that focal points on this topic will be indicated and Vietnam will co-ordinate the activities. As it turned out, Vietnam had some difficulties in organizing the activities, and Indonesia was later requested to take over the initiative. A Group of Experts Meeting (GEM) was held on this topic in Jakarta in November 1998 and the meeting was able to exchange their knowledge on the geology of the South China Sea and agreed to work together with the CCOP in Bangkok to implement the proposal on "Compilation of Geoscience Data of the South China Sea" and the "establishment of geoscience data base for the South China Sea". At this moment the Workshop in establishing contact and co-operation with the CCOP.

With regard to **hydrocarbon** resources, the TWG agreed to "undertake a joint preliminary study of a suitable sedimentary basin in the South China Sea area, without prejudice to claims of individual countries" and that the study "should begin with collation, exchange and interpretation of the available geological, geophysical, and geochemical data that exist in their own countries or could be relatively easily accessed from other sources", and "would be conducted with the long term view of using an appropriate analysis technique for hydrocarbon resource assessment". Indonesia would co-ordinate this activity. Yet, there are various difficulties in implementing this agreement, particularly the sensitive nature of the hydrocarbon resources and many countries regarded the data as confidential

commercial data. So far, not much follow up has taken place on this subject.

With regard to **other resources**, the TWG "recommends the investigation of the feasibility of setting up a marine reserve or marine park in an area to be defined within the multiple claims area". Activities to be considered within the area may include among others joint scientific research and eco-tourism. Some discussion took place in various working groups on this issue but no agreement as yet achieved on this topic, particularly because of the difficulties in defining "the area within the multiple claims" that could be subjected to the joint development of marine park or marine reserve.

With regard to the **non-living resources**, the TWG also found the need:

- a. "to define clearly the area that could be subjected to joint effort in the multiple claims area around the Spratly Islands groups, without prejudice to the various territorial or jurisdictional claims in the area";
- b. "to collect and analyse as much as possible the various concepts of joint development that are already existing, particularly in the region, and to use them, as far as practicable, as models for developing joint efforts regarding the multiple claims area".

The results of the TWG-RAWD were discussed and adopted by the Fourth Workshop in Surabaya in August 1993.

Due to the sensitive nature of the resources issues as the result of the territorial sovereignty claims, it was initially difficult to make progress on this topic. The Fifth Workshop in Bukit Tinggi in

October 1994 further discussed this matter and repeated the recommendation to the respective authorities to identify their respective focal points with whom the coordinators of fisheries (Thailand), hydrocarbon resources (Indonesia) and hard mineral resources (Vietnam) would work to develop the co-operative programs. The nomination of the focal points and the follow-up activities have proven to be somewhat slow.

Only at the Eighth Workshop in Puncak in December 1997 did the Workshop look into this issue again. It decided, among others, that "a study group on zones co-operation, including analyzing of existing joint development arrangements" be convened in the middle of 1998 and that a GEM to study non-living and non-hydrocarbon resources (hard minerals) be convened in October 1998 to further study the matter in order to find co-operative ways for that purpose. Such a study group was held in Vientianne in June 1998. The study group made substantial progress. In this meeting many approaches to maritime co-operation, including various models of the joint development and possibilities were discussed, such as the Malaysia-Thailand and Malaysia-Vietnam agreements, the Indonesian-Australian agreement, the China-Japan fisheries agreement in East China Sea, the situation in the Caspian Sea, the Argentine-United Kingdom agreement in the South West Atlantic, the Antarctic Treaty, and others. It was noted that such concepts were being used increasingly throughout the world including in South East Asia and in the South China Sea to address a variety of issues.

It was also agreed in Vientianne that maritime co-operation, including joint development, has potentials to assist in resolving the difficulties in the South China Sea. Moreover, it was also observed and agreed that:

- a. It could facilitate the development of resources as well as political relations between the parties concerned;
- b. It could contribute to developing confidence building and promote co-operation and the avoidance of conflict and at the same time promote good neighbour policies;
- c. Joint development is provisional in nature, and does not deal with territorial or jurisdictional matters: rather, it is without prejudice to such issues and attempts to circumvent them;
- d. It encourages investment by creating a more certain investment climate;
- e. The various models of joint development indicate that once agreement is reached on the need for this approach, it will take a lot of time and efforts to conclude the joint development arrangement;
- f. Although many joint development arrangements have been formulated in the form of treaties, in all cases the arrangements must be approved or supported by the authorities concerned;
- g. It is important that the authorities concerned be convinced of the utility of joint development arrangements particularly in the disputes areas since this arrangements could be more beneficial to them than the continued disputes or the prolonged inability to develop the area or its resources;

- h. The common objective of any arrangement must be articulated clearly prior to agreement;
- i. Joint development creates opportunities to continue efforts to seek solution on territorial and jurisdictional issues.

The Vientianne meeting also observed that various models of the joint developments also indicated several common elements such as:

- a. The agreed perception that joint development is good for all parties to the dispute and therefore they support them;
- b. Joint development could be formulated without prejudice to territorial or jurisdictional delimitation;
- c. The area of the joint development must be defined through negotiation and on the basis of international law;
- d. The parties to the arrangement should be identified;
- e. The scope for the joint development should be clearly indicated;
- f. The mechanism to implement the arrangement is clearly established by agreement;
- g. Various issues such as the right to tender contract, the problems of applicable laws in the joint development area, problems of criminal and civil jurisdiction as well as issues relating to sharing of expenses and benefits are clearly regulated;
- h. The participation of commercial institutions or companies in the joint development arrangement could be encouraged within the context of promoting commercialization of the joint development arrangement and minimizing political and legal issues.

It was also noted in Vientianne that the scope of an arrangement could include issues of differing sensitivity, such as environmental protection, marine scientific research, safety of navigation, peaceful uses of the sea, utilization and conservation of living resources, and management of non-living/hydrocarbon resources. It should be understood that the concept of joint development should not be limited to the development of non-living resources, but should also cover a much wider scope. It was agreed in Vientianne that further meeting should be convened in 1999 to further discuss in greater detail the issues involved, particularly the issue of management and supervision, including the powers of the joint development authorities, and the civil and criminal jurisdiction aspects. Moreover, the issue of determining and defining the area for the joint development should also be investigated, and some consultation is currently going on in this matter.

The Ninth Workshop in Jakarta in December 1998 discussed and endorsed the decision of the meetings of the study group and the expert group. It was agreed to convene a second meeting of the study group on the zones of co-operation to further explore the topics. Such a meeting was planned to be held in June 1999 in Bali.

It is clear therefore that the concept of joint development is useful and promising in South East Asia and in the South China Sea. The concept is a good way of creating peace and stability in the region. It is very much in line with what the former Chinese Prime Minister Li Peng

said in 1990. The parties concerned are expected to give more time and thought to this concept. On the basis of the decision of the TWG-RAWD in 1993, in 1994 there had been attempted to find out and looked for an "area or a zone" for the joint development effort where those having overlapping multiple claims can co-operate on the basis of UNCLOS 1982. For obvious reasons the suggestion on this subject was never made public, but it had been communicated to all the parties concerned. After some consultations, certain claimants were happy with the suggestion, certain others said that they might have some reservation but were quite willing to discuss it, but there were also some who rejected it immediately. After some further considerations of this topic, particularly after the Vientianne meeting, the joint development or joint co-operation concept was felt to be indispensably further developed and that certain specific area for this endeavour could still be worked out. In this context, the following observation could be useful:

- a. In view of the various statements made by the parties concerned, the area for joint development or joint co-operation should involve the relevant parties. It appears possible that the area could start with a relatively small area involving not so many parties;
- b. The agreement to establish the joint development or joint co-operation should be without prejudice to the respective territorial and jurisdictional claims. For this purpose the joint development should initially start with the involvement of non-official arrangement, including private commercial companies. In the meantime the respective authorities or governments can continue to discuss the territorial and jurisdictional issues;
- c. The participant in the joint development efforts should be those which are directly interested parties and which are maintaining presence in the zone;
- d. The subject for the joint co-operation, at least at the initial stage, should begin with the least controversial matters, such as marine scientific research, protection of the marine environment, developing marine parks, joint ecotourism, joint effort for search and rescue operation, co-operation in providing shelter to fishermen in distress, joint hydrographic and oceanographic surveys, joint effort to combat piracy and trade in narcotic drugs, and so on;
- e. At a later stage, when condition permits, joint co-operation on exploration or even resources exploitation could be attempted as already the case in many joint development agreements;
- f. Joint development could be designed for a specific period, say 40 or 50 years;
- g. The joint development concept should not prejudice the provisions of UNCLOS, particularly regarding islands, enclosed or semi enclosed seas and rocks and reefs;
- h. The current occupation of certain islands in the zone should not be regarded as recognition of territorial rights. By agreements between the parties concerned the occupation could be used for common benefits. The existing installations or structures erected on the

reefs could be used for mutual benefits, such as for fishermen shelter or as basis to conduct co-operative efforts;

- i. The establishment of joint development or joint co-operation zone presupposes that the parties concerned should refrain from further occupation unless agreed by all parties;
- j. It is also presumed that the existing occupied islands, reefs or rocks should not be used for military purposes and that transparency with regard to activities in the occupied reefs would increase the prospect for the development of an effective joint co-operation.

Finally, an appropriate question to ask is: if everyone in the South China Sea agrees that the joint development concept is good and that the practices around the world indicate similar conclusion, why then is it so difficult to apply it in the South China Sea, at least in the heavily contested multiple claims area? The answer to this rather simple question turned out to be more complicated:

- a. It is difficult to precisely know which areas are being claimed by certain countries, and therefore it is difficult to clearly define the disputed area. Some claims are clearly identified by co-ordinates, but it is not clear what are being claimed within the co-ordinates. Some claims are not even well defined by co-ordinates, and what is being claimed within the undefined claims is not clear either;
- b. The roles of islands, rocks and reefs in determining maritime zones. The

UNCLOS 1982 stated in Article 121 (3) that "rocks which cannot sustain human habitation or economic life of their own shall have no EEZ or continental shelf". Some claimants seem to think that by establishing a claim over a rock or reef they can extend their maritime claims to EEZ and continental shelf from that rock or reef. This expectation would be difficult to sustain. Moreover some claimants also seem to think that by erecting structures over a submerged reef they could claim EEZ or continental shelf using the structure as a basis. Again this expectation would be difficult to justify;

- c. Many of the claimants do not seem to take the provisions of "semi enclosed seas" in Article 122 and 123 seriously, particularly the provision that stipulates co-operation in the semi enclosed seas with regard to exploration and exploitation of living resources, protection of the marine environment, marine scientific research activities, and co-operation with other interested states or international organizations on these matters;
- d. Finally, the concept of joint development at this moment seems to mean different things to different people. There is a strong tendency among the claimants that joint development should not be attempted in an area which a claimant believes to be its own, and that the concept should only be used in an area claimed by others or for an area outside of its claims.

International Cronyism -- the Role of the International Monetary Fund and the World Bank*

Helen Hughes

The Development of International Economic Institutions

SINCE World War II international institutions have introduced a new element into "the rules of the game" by which nation states conduct their affairs at home and abroad. The core of the United Nations (UN) family was created in San Francisco before World War II ended. After the war UN membership grew rapidly as colonial countries became independent. Component and associated agencies multiplied as the UN embraced widening agendas.

UN institutions are ruled by a one nation-one vote system. Micro states, with populations of less than 100,000 have the same weight as mega states with populations of several hundred million. Democratic controls, representing weights of voters and taxpayers, can not be exercised. The Security Council is a significant exception. The interests of voters have been recognized in its core permanent representation of large states and in the ability of

major countries to exercise a veto in Council proceedings.

A "quota" national representation system rules UN staff selection formally at lower levels and informally at senior management levels. Large countries and geographic groups of countries (such as sub-Saharan Africa, the Middle East and Latin America) take turns in senior jobs.

The World Bank and the International Monetary Fund (IMF) were created in 1944 at the Bretton Woods Conference.¹ Membership of these two institutions is by financial subscriptions that are weighted by the members' economic strength. Members have to conform to the Articles of Agreement which prescribe rules of behaviour, including economic reporting to ensure openness. The two institutions are managed by Boards of Executive Directors (and their Alternates) representing the major member countries and groups of smaller ones. Votes reflect the level of subscriptions. Executive Directors act

*Paper presented at the Mont Pelerin Society Special Regional Meeting: Liberty, Culture and Institutions -- Paths to Economic Progress in Asia, Bali, Indonesia, 8-11 July 1999.

¹They are located in the capital of the largest subscriber, presently Washington DC. Further unification of the EU could lead to proposals that the two institutions, with the bountiful rents they bring to their location, move to a European capital.

on instructions from their Treasuries/Ministries of Finance and, or, Central Banks, although in practice have a great deal of freedom in their contributions to the Board debates. The managements of both institutions, headed by the President of the World Bank (currently James Wolfhenson) and the Managing Director of the IMF (currently Michel Camdessus), in practice dominate proceedings, initiating and implementing lending and associated policies. While debates do take place, governance is dominantly by consensus that almost always supports management views. Formal divisions are extremely rare. Regional multilateral development banks for Latin America, Asia and Africa are structured similarly.

The General Agreement on Tariffs and Trade (GATT) was formed in 1948, and did not become the World Trade Organization (WTO) until 1995. It is self-selected by adherence to its Articles of Agreement. The WTO is governed on a one nation-one vote basis, but country representatives in Geneva play an important role in its direction (Henderson 1998). The WTO proceeds by detailed negotiation on tariffs and other trade issues, involving member countries, notably in its multilateral trade liberalization Rounds.

Trade liberalization was a key component of the attempt to restructure the fascist corporatist states and prevent a replay of 1920s and 1930s protectionism. The establishment of an international institution with this objective, nevertheless, proved impossible. The 1948 interim compromise was the GATT. The concept of a World Trade Office was to lie on the

agenda for 50 years. GATT's early success in initiating tariff reduction among industrial countries was due to United States' use of its international economic strength to bring the other industrial countries to the negotiating table. With some 40 per cent of the industrial countries' GDP, and as the dominant donor to West European and Japanese post-war reconstruction, the United States carried the weight necessary to turn the protectionism of the 1930s toward internal and external liberalization. United States commercial interest benefited from the technological lead created by its war economy, so that free trade views were widely accepted, notably by multinational corporations that were spreading their interests to Europe and the emerging countries. The Dillon, Kennedy and Tokyo Rounds of multilateral trade negotiations within the GATT framework were a triumph for United States hegemony, reducing tariffs on manufactured goods to negligible proportions in industrial countries.

Codes that would reduce the use of non-tariff barriers were also successfully negotiated in the Kennedy Round, but were not implemented. The GATT was emerging as mercantilist in spirit, focusing on freeing up exports rather than on promoting free trade. Subsequent attempts to improve member nations' adherence to free trade principles have underlined the residues of protectionism, notably on non-tariff issues. The Uruguay Round, attempting to tackle new ground in agriculture and services, achieved less than previous Rounds that were mostly concerned with manufacturing. Agricultural protectionism in Europe and Japan stimulated increasing protec-

tion in agriculture in the United States and in developing countries such as Taiwan and the Republic of Korea. The reduction of protection in services does not led itself to the same clear cut liberalization processes as the reduction of tariffs on manufactured goods. Even in manufacturing, protectionism has returned in new guises in its attempts to use "fair trade" and environmental issues to roll back trade liberalization.

The failure to establish a trade "organization" had a number of advantages. Member countries kept a close watch on GATT negotiations. The number of staff and their self-perpetuating activities, such as research and public relations, was kept within bounds, though the introduction of surveillance reporting reflected bureaucratic expansionism that has become widespread in international organizations. Several UN agencies, the IMF, the World Bank, the regional development banks and the OECD prepare a wide range of global, regional and country surveillance reports. Because they are subject to bureaucratic standards of political correctness, they are highly repetitive, far from rigorous and have consistently failed to predict world or national trends. Their audiences are too small to justify their contribution to the felling of forests. It will be interesting to see whether the WTO can maintain the levels of effectiveness of its predecessor or whether it will continue to expand into peripheral activities as other international institutions have done.

The rise of regionalism, in opposition to the spirit of world free trade enshrined in the GATT/WTO Articles of Agreement,

has been reflected in a mushrooming of regional *juntas*. The Commission of the European Union (EU) is the largest of these and has the greatest supra-national powers. Whether its overall long-term policy impact has been more positive than negative is open to debate. Relations with the Lome group of African, Pacific and Caribbean countries (ACP) and Mediterranean countries enshrined colonial attitudes. The EU aid has had many other negative aspects. The introduction of the uniform Euro currency is even more open to question. Most developing country regional organizations were protectionist and failed (Balassa and Stoutsjidik 1976). The Association of South East Asian Nations (ASEAN) has been an exception, in particular because to date it has largely avoided economic action. It is principally a political organization.

The Organization for Economic and Social Development (OECD) is a self-selected club of rich nations now trying to attract developing countries. The Republic of Korea and Mexico were flattered to be asked, but have already been subjected to pressure to follow policies that are proving counter-productive in high income countries, let alone in low income countries. For example, both countries have been urged to introduce unemployment relief payment systems. Singapore, sensibly took the Groucho Marx view of OECD membership.²

International institution building was undertaken with the best of intentions at the end of World War II. The initial impetus was for lasting peace, national independence for colonial countries and rapid

²"Any club that would want to have me as a member I would not want to join".

economic growth, particularly for poor countries. The technological advances that put world news on everyman's television screens, radios and in newspapers accelerated the internationalization of public debates. A rapidly growing international environment of news reportage and comment strengthened the arguments for the development of international institutions. Advances in the liberalization of international trade and of capital markets were made. New economic, social, political and environmental agendas were developed and debated. The latest development in the international arena has been the use of the Internet to promote the special interest agendas of non-government organizations (NGOs).

Although international agencies flood the media with statistics, they are curiously coy about their own essential data. Some benchmark data collected by David Henderson indicate orders of magnitude for leading non-UN agencies in the middle 1990s (see Table 1).

New International rules and norms of public behaviour have led to positive res-

ults in increasing attention to civil liberties, political democracy and liberal economic policies that created a vastly enhanced growth potential in industrial and developing countries. Countries that adopted liberal economic policies and took advantage of the increasing liberalization of the international environment, grew at unprecedentedly high rates during the last 50 years. They include states as small as Singapore and Hong Kong and as large as the United States. But some countries' per capita GDP has fallen, living standards in many countries have stagnated, conflict within and across national borders has persisted and so has political repression. Overall economic, civil and liberal goal posts, nevertheless, have been steadily been widened and moved forward with beneficial effects for millions of people. Following UN peacekeeping endeavours within several African countries, the Gulf war was a seminal step in international intervention following the Iraqi invasion of Kuwait. Ruthless authoritarian political behaviour has ceased to be respectable within countries, The North Atlantic Treaty Organization (NATO) intervention in Kosovo with subsequent UN support has

Table 1

STAFF NUMBERS AND BUDGETS OF LEADING INTERNATIONAL AGENCIES C. 1995

Institution	Staff Numbers	Administrative Budget (millions of US dollars)	Cost/Staff Member (thousands US dollars)
IMF	2,200	470	214
World Bank	5,700	1,375	241
EU Commission	21,000	3,400	162
OECD	1,700	340	200
WTO	510	97	190

Source: Henderson D. 1998. International Agencies and Cross Border Liberalization: The WTO in Context, in A. O. Krueger; *The WTO As An International Organisation*. (Chicago: The University of Chicago Press).

shown that protecting civil rights in small countries has become achievable.

The growth of international institution and their activities during the last 50 years thus has many facets. This paper, because it focuses on the IMF and the World Bank, deals only with economic aspects. Here it appears that the results of international intervention have fallen far short of the potential and have frequently been counter-productive.

During the late 1940s and 1950s, as Japan and Europe reconstructed on market oriented and liberal lines with the help of the United States, Marxist and corporatist *dirigiste* views dominated economic development in centrally planned economies and in developing countries. The UN and its agencies adopted these views and played an important role in disseminating them.

The International Labour Organization (ILO), that had a pre-World War II institutional history, despite its tri-partite governance by employers, trade unions and national governments, began to develop a detailed agenda for national policies based on Marxist doctrines that it applied to countries at all levels of development. For developing countries, the results were often disastrous. Formal sector employees benefited from the application of ILO rules where protectionist policies made dual wage structures possible. But such economies failed to grow overall, leaving most of the population with very low living standards. Other UN international and regional agencies promoted *dirigiste* policies counter to the market oriented policies espoused by the OECD, the IMF, the World Bank and GATT. "Develop-

ment economics" was the dominant UN philosophy. It was encapsulated by the Prebisch-Singer model of development (Little 1982, Lal 1997). The Economic Commission for Latin America (ECLA) vigorously supported the adoption of statist, protectionist, and *dirigiste* Prebisch-Singer economic management. These led to the creation of corporatist (crony capitalist) economic structures that skewed the ensuing limited economic development to benefit upper income groups, that entrenched poverty and that set the stage for criminality. Those who benefited from the corporatist distortions were able to delay the adoption of liberal economic reforms (except in Chile) well beyond the point at which the sheer incompetence of "development economics" was exposed. The UN Economic and Social Council (ECOSOC) in New York, the Committee on Trade and Development (UNCTAD) in Geneva and the UN Industrial Development Organization (UNIDO) in Vienna were also front runners in promoting the Prebisch-Singer model in developing countries in the 1960s and 1970s. The Economic Commission for Asia and the Far East, later the Economic and Social Commission for Asia and the Pacific (ESCAP), supported counterproductive economic and social policies in South Asia. It was less successful in the face of strong national support, assisted by the United States, and from the 1960s to the 1980s by the World Bank and the IMF, for liberal economics in the East Asian market.

Inward oriented, protectionist national and regional policies were taken up by the UN and its institutions to the great cost of developing countries. The pro-

ponents of the "New International Economic Order", led by the "Group of 77" developing countries, attempted to derail the liberalization of international trade and capital flows during the 1970s, through their influence in the UN and UN specialised agencies. Taxpayers' funds from rich and poor countries were thus channelled through the UN to perpetuate poverty through *dirigiste* policies. The cost of these policy interventions by the UN and its agencies has not been counted. The ultimate responsibility was of course, that of national governments that opted for policies that led to economic stagnation and poverty, but the UN agencies must bear a great deal of the blame for making the Prebisch-Singer approach to development politically correct. Millions of people were cheated of years of life because standards of living failed to improve. If China, India and other poor countries had adopted the liberal economic policies that the UN agencies excoriated in the 1950s, 1960s and 1970s, their living standards would by the 1990s have paralleled those achieved in the mid-1990s by the East Asian economies that took liberal paths to economic development. The scourge of poverty would have been driven into small corners.

"Development economists" persuaded developing countries to abstain from the trade liberalization through the GATT Rounds of multilateral trade negotiations, that with the associated freeing of capital markets, and to a limited extent even of labour markets, enabled the industrial countries to grow at unprecedentedly high rates to reach today's high living standards. Where market orientation prevails, unem-

ployment and the associated incidence of poverty are low. Market oriented East Asian countries benefited greatly from their liberalization of economic policies and grew rapidly with the most substantial reduction of poverty ever experienced in world history. Although the IMF and the World Bank came under attack from "development economists" (Heyter 1971, Heyter and Watson 1985, Chossudovsky 1997), their financial capacities enabled them to use their packages of lending and policy advice to mitigate some of the worst policy excesses of statism and protectionism. In East Asian market economies, their support for local technocrats who rejected the "development economics" strategies in favour of liberal economics was often a key factor in the adoption of liberal reforms.

By the 1980s, and particularly after the collapse of central planning in China and Eastern Europe, the ideological disputes, on the surface, lost much of their vigour. The ECOSOC, UNCTAD, UNIDO and the regional Commissions began to support trade expansion, albeit mostly in a "mixed" (or rather, mixed-up) model. Exporters were granted "incentives" (subsidies) to enable statism, import substitution and industry policies to continue and to build "crony" capitalist economies in domestic markets side by side with competitive export sectors. *Dirigisme* was thus not abandoned. It merely changed its rhetoric. Following the "Japan Inc." growth model being promoted in East Asian market and transitional economies, *dirigiste* policies continued to support the considerable and growing rents accruing to "crony capitalists" and their political and

bureaucratic supporters. Dual economies, composed of internationally competitive export sectors and monopolistic, high cost, domestic production supported by continuing protection, "industry policies", financial "repression" and distorted macro-economic policies, laid the foundations of the 1997 currency and financial crises in Thailand, the Republic of Korea, Malaysia and Indonesia (Hughes 1995, 1999). Increasingly democratic political environments, paradoxically, pressed Ministries of Finance and the Central Banks of the Republic of Korea and Thailand that had defended market values for currencies until the mid-1980s against predatory "crony capitalists", to maintain overvalued currencies to defend the cronies' assets. Cronies were able to use financial reforms for private profit. Foreign capital inflows were encouraged regardless of their destination. They often flowed into highly protected, inefficient industries like motor vehicles and white goods.

It was clear from Hong Kong's success in the 1960s, that while liberal policies led to rapid growth and the alleviation of poverty, *dirigiste* policies resulted in unsuccessful "stop-go" development marked by internal and external crises and sharply differentiated distributions in income. A large volume of rigorous research that documented these trends failed to persuade the UN agencies to abandon their support for *dirigism*. The perseverance of poverty was, however, seized on to justify the continuation of aid by new "direct" approaches to poverty alleviation. *Dirigiste* policies found a new justification, unfortunately with the same absence of results either in growth or poverty alleviation.

The reasons why most international institutions have failed their constituents, and particularly developing countries, in promoting economic growth, are embedded in institutional structures heavily biased against political, financial and economic accountability. Most of the international institutions operate without the parliamentary surveillance that democratic countries, with parliaments subject to elections, carry out as a matter of course. Where resident national missions exercise considerable surveillance, notably over the OECD in Paris and the WTO in Geneva (Henderson 1998), policies have not become distorted to reflect *dirigiste* views. But in the 1990s the World Bank and the IMF, under pressure to create roles for themselves in a world of increasingly open and competitive trade in goods and services and flourishing capital markets, joined the *dirigistes* to maintain their reason for existing.

The bureaucratic practices of the international institutions have also contributed to their retreat from liberal economic values. Their staff recruitment and promotion methods do not stress efficiency and competitiveness. All international institutions pay some attention, explicitly in the case of the UN and EU, and implicitly in others, to their officials' national origin. Staff selection and promotion are not primarily by merit. "Quota" factors also operate in the selection of consultants and contractors. Professionalism, experience and excellence are often sacrificed to mediocrity and rent seeking.

As the international institutions, like national public services, do not have a profitability "bottom line", they use proced-

ural rules to try to minimize inefficiency and corruption. Bureaucratic are pervasive but often arcane. Accounting checks are at best audits, relating expenditures to given targets, not to cost efficiency and project and programme effectiveness. Management reviews of staff performance, given that in effect staff have tenure, are at best feeble.

The staff members of international institutions receive large rents. Entry salaries compete with private sectors in high income countries and are topped up with many public sector privileges. The international organizations provide many subsidies for staff families. The higher the rank of international officials is, the greater the salary and related benefits will be. Senior public servants and politicians in member countries support high remuneration for international public servants. For some national bureaucrats a spell in one of the international institutions as staff members or as consultants beckons. For politicians international institutions are places where they can place themselves or their cronies without cost to their own country. In some countries privileges continue when staff retire from international institutions. International salaries are paid net of tax under complex arrangements that avoid unnecessary transfers between member governments and international institutions. Retirement pensions normally become fully taxable under these rules. Some countries, however, do not levy taxes on international institutions' pensions. India is a prime example. Former Indian employees of international organizations, who are among the highest income earners in India, are thus exempted from taxes on their pensions!

Permanent tenure is a significant aspect of the rents earned by the staff of international institutions. "Platinum" handshakes are necessary to shake out inefficient staff. Outstandingly productive performers, who, in contrast to their mediocre and unproductive colleagues, are not overpaid, tend to leave in protest against excessive bureaucracy. Mediocre and poorly performing staff remain to form the top echelons of management. The staff morale of international institutions is inevitably, but not surprisingly, low.

Reviews and evaluations of international institutions are carried out from time to time, sometimes on regular schedules, but sometimes in response to exposures of egregious waste of resources or negative project or programme impacts. International bureaucrats are at their best in such situations. They spring into action. No care is spared. Long hours are worked. The world is searched for reviewers who will provide a correct mix of scepticism and critical comment but, fundamentally, provide support for the institution being reviewed. Persuasive documents are prepared for the reviewers. Great efforts are made to ensure that a final report is sufficiently critical to indicate that some reorganization is necessary, but so supportive that an institution or its component agencies will survive, and hopefully, even be able to access additional taxpayers' funds. The 50th anniversary reviews of the Bretton Woods institutions were masterpieces of this *genre*. "Development economics" made a comeback, remaining somewhat critical, but coming out strongly for survival of the IMF and the World Bank.

International institutions that have outlived their functions become dependent on support outside the democratically elected parliaments that become critical of their role. NGOs in industrial countries have thus come to play a key role in the policies of international institutions. Free of the constraints of Marxist parties, their effectiveness has been greatly improved by the use of Internet international networks to further their agendas. The recent NGO's attack on the Multilateral Agreement on Investment showed that Marxist views about private direct foreign investment are still strong enough to sink liberal initiatives (Henderson 1999). The pursuit of simplistic, populist solutions to complex economic, social and political problems has been able to generate popular support since the days of peasant revolts, unfortunately at tremendous cost to those they claim to intend to help. Coalitions of "one cause" groups are particularly effective in the international arena by stripping down to slogans the detailed arguments required to conduct rational debates in national political arenas. At the same time they claim that their rights to direct representation in international debates should supercede national, democratically elected parliaments.

The efficiency and effectiveness of the World Bank and the IMF have to be seen in the context of policies and activities of international institutions during the past half-century. In such an overview, the two Bretton Woods institutions, at least in their early years, made more positive contributions, and were less counterproductive, than most of the UN family of international institutions. But the IMF and World

Bank roles have changed as the liberalization of world markets has taken away the reasons for their existence.

IMF

The discussions that led to the Bretton Woods meeting in 1944 were intended to create new international economic frameworks that would avoid the destructive "beggar my neighbour" policies that had led to, and increased the severity of, the 1930s depression. The depression was seen as a major cause of the rise of fascism so that the Bretton Woods conference had strong political backing from the victorious democracies. Current account liberalization was seen as a necessary parallel to trade liberalization. Just as the times did not permit the creation of an International Trade Organization to enforce free trade, the theories and practices of the day led to a world of fixed, rather than floating, exchange rates. The IMF was created to act as a central bank for the central banks of member countries. It was to provide financial support to enable countries to avoid competitive exchange rate devaluations that would destabilize international monetary flows. The IMF function was to advance short term credits to countries in difficulties through internal (budget) and external (balance of payments) deficits. It was clearly recognized that such deficits resulted from inappropriate national policies. The IMF was to assist countries to identify the causes of their economic problems and to remedy them through policy reform. To this end a surveillance system, consisting of IMF (confidential) reports that would be ap-

proved by the IMF Board of Directors, followed by discussions between IMF and national financial officials was instituted, initially for countries in difficulties but eventually for all member countries. Exchange rate changes could be undertaken after IMF approval.

The IMF was organized by country divisions grouped into regional departments. If a country needed assistance, national and IMF staff worked out the extent of the assistance required in the form of short term (generally 3 year) credits that would enable budget and balance of payment policy reforms to bring the country back into balance. The disbursement of credit tranches was dependent on conformity with the agreed policy reforms. Conditionally was thus short-term and could be monitored. If countries did not comply, drawings of credit tranches would not go ahead. Although the quality of surveillance, conditionally conditions and credit practices varied, as did country compliance, given fixed exchange rates, the IMF interventions were on the whole useful. National technocrats were often able to implement reforms that threatened the rents of privileged groups by making it appear that it was the IMF that was responsible for the reforms that they wanted to initiate. The IMF was also a convenient scapegoat for politicians who wanted to shift the blame for economic downturns that resulted from their policies.

From the point of view of IMF staff, this was a golden age. When industrial and developing countries sought IMF credits, they bent over backwards to provide IMF staff with red carpet treatment. Receptions, banquets and official and pri-

vate travel in luxury government cars were par for the course. But these were minor luxuries compared to the intellectual advantages represented by IMF staff access to research and analysis that country officials, thinly spread over a vast range of immediate problems, could only envy. The IMF -- country analyses and dialogues were thus effective forms of technical assistance but they unfortunately also encouraged mandarin attitudes among IMF staff. A Washington orientation was encouraged so that local analytical development was neglected. As the education and skills of the Ministry of Finance/Treasury/Central Bank officials with whom the IMF staff conducted negotiations improved with graduate studies abroad, mainly in the United States, and as local research began to develop, the IMF fell behind in its analytical inputs. It was often still useful to have outsiders with plenty of technical resources to contribute to policy dialogues, but the specificity of local economic knowledge and political understanding was lacking. The relative value of analytical technical assistance declined.

The Bretton Woods "architecture" (to use current jargon) collapsed when it became evident that fixed exchange rates were out of date. When floating exchange rate superseded fix exchange rates, the IMF lost the function for which it had been founded. The staff proceeded to carve out new roles to perpetuate the institution.

Short term credits continued to support countries with policies so inappropriate that they resulted in internal and external crises. IMF lending became concentrated to a relatively small group of de-

veloping countries that avoided long term policy reform, becoming "addicted" to IMF "rescues". IMF lending expanded, providing resources for expanding country interventions, research and a public relations effort aimed that aimed to sell the IMF as a key agency in international capital markets. Promoting private and public capital flows to developing countries became a more important message than the liberal policy reforms needed to enable such flows to be productive.

At the end of the 1960s when predictions of a global shortage of capital became fashionable, the IMF saw an opportunity to promote its role by the creation of Special Drawing Rights (SDRs). These were to provide the world with adequately liquid reserves and the IMF with a new central banking function. SDRs were to become country's international reserves and hopefully the world reserve currency. The IMF mandarins misjudged the situation. Capital markets solved an apparent liquidity problem. The European countries' creation of Eurodollars to circumvent US capital market restrictions, followed by US capital market liberalization, enabled capital markets to expand rapidly. National monetary managers proved unable to contain the inflation that arose from the boost that commodity, notably petroleum, price rises gave to credit creation. The IMF's attempt to create a new global currency failed. Although much of the IMF's voluminous reporting is in SDR's, their practical use is negligible. They form about 2 per cent of total national reserves.

The first flush of *hubris* in the expansion of capital markets in the 1970s enabled countries with grossly distorted domestic economic policies to borrow abroad

from private lenders. When the combination of careless borrowers with careless lenders precipitated debt "crises", the IMF sought to protect the public and private borrowers, mainly in developing countries, and the private lenders, mainly industrial and petroleum rich countries, from the consequences of their actions. Instead of writing off the debt and thus forcing policy changes, the IMF led the bailouts that would push most of the costs of bad loans onto developing country taxpayers. In the jargon of the day, this was called socializing the external debts. Developing country taxpayers were predominantly low income groups that paid indirect taxes and were taxed by the inflation that the socializing of debt permitted to continue. The IMF's Board, closely linked to the financial sectors in industrial and developing countries in the absence of democratic surveillance, did not protest when the management brought the rescue packages to it.

At the end of the 1970s, total private and public lending to developing (and communist) countries was only about 10 per cent of the total global domestic and international lending. The international financial system would not have collapsed if the private lenders would have had to take the full consequences of their foolish lending. The debt "crises" of the 1970s and 1980s were mainly Latin American. Several Latin American countries would have had to adopt policy reforms more thoroughly and expeditiously with considerable long-term benefits if the IMF had led in the socialization of their debt.

By seeking to sweep the origins of debt "crises" under the carpet and rescuing borrowers and lenders, the IMF intro-

duced severe "moral hazard" into international capital markets. It soon became evident that no matter how egregiously irresponsible governments were, the IMF (supported by the World Bank) would make sure that they were not held responsible. In most highly indebted countries, governments had created high inflation, thus encouraging capital flight. Such funds were safely and profitably invested in international capital markets. A number of governments encouraged the cronies who were transferring the profits of their protected and subsidized enterprises abroad, at the same time to borrow abroad with considerable exchange rate risk. Guaranteeing private loans from foreign sources eliminated the risks. Much of this borrowing again flowed into protected and monopolistic industries owned by the cronies who were being subsidized by *dirigiste* policies. When subsidies caused budget difficulties, the IMF (and the World Bank) came to the rescue.

Growing recourse to government borrowing abroad necessitated an expansion of surveillance reporting that exceeded the analytical ability of staff. Rigorous economic analysis that had made the case for continuous liberal reform as a basis for rapid long-term growth gave way to short-term "adjustment" to external shocks. The IMF here took its lead from the World Bank which mastered the "adjustment analysis" quickly and extensively to meet its lending problems (see below). Blaming "external shocks" instead of domestic policies for debt and currency and other financial "crises" provided the intellectual justification for the moral hazard being fostered by the IMF in international capital markets.

By the 1980s the only developing countries that sought the IMF's assistance were those unable or unwilling to reform their economic policies. The collapse of central planning in China and Eastern Europe at the end of the 1980s fortunately for the IMF's existence expanded their number. Political considerations in industrial countries put pressure on the IMF (and the World Bank) to expand funding to the economies in transition regardless of analytical procedures and without much regard for conditionality. While European countries feared vast immigrations if the problems of the East European countries were not contained. While it is admittedly extremely difficult to reform and reconstruct centrally planned economies, the IMF and the World Bank have not been able to intervene so as to make the transition processes even moderately effective, particularly where central planning was entrenched since the 1920s. The transition has not been to competitive markets but to corporatist capitalism with high criminal content and disastrous effects on living standards. On present indications, IMF lending will only be repaid by taxing low income groups.

Mexico is a dual economy, with efficient export industries and vastly inefficient, protected and monopolized domestic sectors. It was a major IMF credit recipient in the mid-1980s. Unwilling to carry out essential reforms, Mexico became more and more dependent on the availability of IMF funds. There was in effect no conditionality. A \$16 billion credit in 1995 to support yet another currency and financial collapse, was clearly the result of years of mismanagement aggravated by extremes of crony corporatism which previous IMF credits ig-

nored. The aim was to rescue Mexican borrowers and industrial country lenders, albeit at the cost of Mexican taxpayers. The US Department of the Treasury and the Federal Reserve, perhaps understandably for political reasons, but unfortunately for Mexico, condoned the IMF escalation of support for careless borrowers and lenders.

The prediction that the Mexico rescue would be a major contributor to moral hazard in international capital markets was amply illustrated in East Asia. Despite the engagement of formidable surveillance resources, including the residence of staff in Indonesia, the IMF failed to anticipate the currency and financial collapses in Thailand, the Republic of Korea, Malaysia and Thailand. Indeed, it substantially contributed to them in two ways. The IMF strongly promoted the flow of capital to the developing countries of East Asia, failing to distinguish between capital flows that strengthened their economies and negative flows that went to inefficient crony corporatist groups. The IMF's failed to analyse and publicize the evolution of dual economies even as efficient export sectors were becoming swamped by monopolistic, inward oriented domestic economies. The subsequent economic collapse in Brazil was equally unanticipated, although Brazil's determined failure to implement macroeconomic reform has led to such episodes at least once a decade. The Russian currency collapse was even more predictable, given domestic policies.

The currency and financial aspects of the 1997 "crises" in Thailand, the Republic of Korea, Malaysia and Indonesia have been thoroughly discussed (McLeod and Garnaut 1998, Montez and Popov 1999, and Hill and Arndt 1999). The underlying

problems, as crony capitalism in the domestic economy swamped the efficient export sectors and began to dominate macroeconomic policy have also been noted (Hughes 1999). The IMF's reports before the collapses of 1997, subsequent analyses and analyses of the rest of the East Asian economies have failed their surveillance task both for the countries concerned and for lenders to those countries. IMF "conditionality" has therefore not made an incisive contribution to the debate that would help to make the reforms effective. While the situation varies among the three countries (Thailand, the Republic of Korea and Indonesia) that have sought assistance on a large scale, there is no evidence that reform that would deal with the underlying problems are being tackled. It is clear, however, that the IMF is satisfied. Stanley Fischer, First Deputy Managing Director, reported to the IMF Board on progress on its US\$10 billion accommodation to Indonesia (further supported by the World Bank, Asian Development Bank and bilateral donors). In 21 March 1999 Fischer claimed that "Policy implementation has continued to be satisfactory since the last review completed in December 1998, and the major macroeconomic targets under the programme for 1998/1999 have been met. Monetary policy has remained firm, while fiscal policy has started to provide the stimulus to the economy, primarily through increased spending on the social safety net" (*IMF Survey*, 28(7): 98, 5 April 1999). The Republic of Korea and Thailand are also being patched up for further IMF dependency.

The least well managed countries, notably those in sub-Saharan Africa that had borrowed to finance the consumption of

their elites had such large private and public debts that they could no longer afford to service their debts, let alone borrow further. The Paris Club was formed to enable industrial countries to "forgive" low income countries public debt owed to donor governments, that is, debt incurred in the form of aid loans. The aim was to provide a structured environment for forgiving aid so that government that persisted with inappropriate policies, wasting aid flows, could not simply write off their debt, not reform their policies and borrow again. A great deal of debt has been forgiven in this context. But the NGO argument is that all debt, private and public should be forgiven regardless of national economic policies. Support by the IMF, the World Bank and other international agencies of this approach will introduce even greater moral hazard into low income countries' economic management. Private lending to them will dry up. Is this the NGO objective? Is it the IMF and World Bank objective?

The IMF is preoccupied with the need to reform the international financial system although it was the competitiveness of that system that put a stop to egregiously counterproductive lending that threatened to push East Asia onto a Latin American path of development. Issues of international financial architecture feature prominently. IMF staff has not examined or acknowledged its past and continuing failures in East Asia. On the contrary it has used these countries' problems to further its own ambitions. The concept of "contagion" is being used to argue for more intervention in international capital markets. The idea that international capital markets are "too efficient" and

need some "sand in the machinery" to make central banks' tasks easier, seems fortunately to have been abandoned as an argument for greater control by the IMF. A new Arrangements to Borrow programme has been introduced, however, to strengthen the IMF's role as a lender of last resort. Although the new Arrangements include some wording about conditionality, given the IMF's record, the main effect is clearly to extend lending.

The World Bank

The World Bank and the IMF were mis-named. While the IMF is primarily an international central bank to serve national central banks, the World Bank was established as a development fund that would provide finance for clearly identified projects that would assist development. All loans would be to central governments to ensure repayment. After a brief period of funding post World War II reconstruction for countries such as Austria, Finland, the Netherlands, Japan and, amazingly, Australia, the World Bank began to fund the foreign (scarce) exchange components for major development projects in developing countries. The rationale was that the World Bank could borrow at lower interest rates than its member countries in the then barely emerging capital markets, because its borrowing was in effect guaranteed by its member industrial countries. It could lend for longer terms of 10 to 30 years. World Bank lending was to developing country governments, though lending instruments were devised to enable funds to be on-lent by specialized public and private institutions to farmers and businesses. Typically these were used

to avoid the necessity of liberalizing financial markets. Lending was, in keeping with the philosophy of the times, at subsidized interest rates.

As the World Bank expanded its lending, it developed a number of component institutions. The first major one, the International Finance Corporation (IFC) was created in 1956 to channel equity and loan funds to private businesses, mainly in the form of joint ventures. The IFC led the demand for protect and for monopolistic privileges in developing countries in the 1960s although it repositioned itself with somewhat more market oriented views in the 1970s. Its main function has been the public relations one of showing that the World Bank had a private sector agenda. The IFC's lending has not been large either per project or in total, but it has largely replaced other sources of private funding. Its technical assistance has been of limited value with many IFC projects being slow and subject to many difficulties.

In 1960 industrial member countries were asked to make contributions to an International Development Agency (IDA) fund to enable loans to be made at very low interest rates and for long periods to extremely poor countries not deemed credit-worthy for standard World Bank loans. World Bank profits were to go to IDA.

Other off-shoots include an Economic Development Institute to top-up the skills of middle level government officials at a time when most lacked appropriate tertiary training (The IMF had a parallel training for finance officials from developing countries). The World Bank also created an

institution for the settlement of disputes arising out of foreign investment.

It soon became evident that the Bank had to assist its clients with technical and financial project analysis to ensure that the projects it funded were viable. But no matter how viable, projects could not thrive if national economic management was distorted. Sectoral and national economic reviews had to be undertaken to ensure that the projects for which loans were made were not only technically and financially sound, but were justified from a national economic point of view. These essentially microeconomic and institutional studies complemented the IMF's macroeconomic surveillance, although there was a great deal of overlap. Sometimes, to the amusement of clients, because communication between the IMF and World Bank mandarins was notoriously poor, the two institutions disagreed on the details of their advice.

The World Bank also had to contribute to project appraisal and implementation. In these "hard hat" activities the World Bank often made its most valuable contributions in its early years. The Bank's costs were covered by interest rate surcharges over borrowing rates. In general, developing countries, nevertheless, obtained lower total interest rates through World Bank borrowing than by going to thin early international capital markets. The World Bank's packaging extended the life of loans beyond commercial terms.

The World Bank's operations were grouped geographically. The individual borrowing country was the core component. The objective was to go from overall

evaluation of the economy in each country to sectoral analyses and hence to the selection of projects most in need of foreign exchange support and likely to make the greatest contribution to growth and development. Technical, financial and economic project analysis methodologies were developed. Institutions were built to enable projects such as roads or power generation could be sustained. All these steps were necessary to ensure that borrowers could service and pay back their loans. Lending to countries in the grip of *dirigiste* policies thus not only involved specific project conditions, but also economy and sector wide discussions to ensure that economic policy discussions could be held at high levels. Some countries welcomed this approach, with local technocrats taking advantage of World Bank as of IMF pressures to push reforms they regarded as important. They did not always succeed in persuading politicians that reforms were necessary, but, notably in several East Asian countries, progress was made. World Bank conditionality was concerned with long-term economic changes and therefore could not be monitored over the short run. Effective conditionality depended on long-term relationships between World Bank country staff and developing country officials. It also depended on the World Bank being willing to cut its lending programmes and even withholding loans if countries did not want to meet project and policy conditions.

In practice, economic analyses and technical inputs were the subject of detailed and often prolonged negotiations. Technical assistance and economic analysis had substantial learning components. The activities of the World Bank as of the

IMF greatly improved data bases and assisted in the training of statisticians, economists, financial analysts and other professionals. The countries improved their information bases. Both developing country and Bank staff improved their understanding of development. Academics, mainly from the United States, who taught development programmes and worked in developing countries, and their students, contributed to the strengthening of knowledge about development. In the 1960s, when George Woods became President, the World Bank moved toward liberal economic stances that enabled it to make a substantial contribution to the liberalization of the East Asian economies and mitigated the inward oriented and statist *dirigisme* of other countries. In the 1970s the World Bank developed central technical and economic analytical and research programmes. The networks created spread beyond the United States to Europe and to developing countries. Project technical analysis and country and sector economic work was subject to World Bank wide reviews by appropriate specialists. As documents progressed from "white" to "yellow", "green" and ultimately "grey" revisions, rigour was sacrificed to sparing national feelings, but the points had often been made when the drafts were discussed with developing country bureaucrats and politicians. At its peak, in the early 1970s, the World Bank made serious inputs into development thinking and practices.

Rapid expansion of World Bank borrowing after Robert McNamara became the President in 1968 had positive and negative aspects. Financial resources ceased to be a constraint on Bank activities. If

staff were incompetent, they could be moved aside and new staff could be hired. Analytical and research undertakings flourished. The use of consultants grew. The World Bank became the central locus of analytical work on development for other international institutions, for national and international aid donor agencies and for developing countries. The speed and the extent of growth was so great that "many flowers" were able to bloom within the Bank. A wide range of hypotheses flourished but analytical work and research were initially mainly focused on economic growth related areas.

Rapid expansion, however, also had costs. The size of the lending program remained the principal incentive for World Bank staff. As the pressure to lend more grew during Robert McNamara's Presidency, analytical contributions to the lending projects declined. For example, the World Bank wide reviews of country economic analyses were ended. The inevitable partisanship of country staff ceased to be subject to Bank wide critique. Country and regional managers cut corners to increase their lending throughout. Conditionally went out of the window. No matter how inappropriate their policies, countries were not refused loans. World Bank loans flowed into the corporate capitalist countries of Latin America, into crony capitalist Philippines in East Asia, into chronically mismanaged countries like Egypt in the Middle East and into the basket case sub-Saharan African countries. Counterproductive policies in Tanzania were complemented by loans to disgracefully unproductive agricultural projects.

The expansion of aid flows, including the expansion of lending by the World

Bank, did not accelerate growth and development as the aid lobbies, basing themselves on savings and foreign exchange gap theories, argued. The slow domestic slog of policy improvement to stimulate increasing productivity, saving and investment and hence productive employment and living standards, was clearly the only path to development. This model was demonstrably working in several East Asian countries in terms both of rapid growth and poverty alleviation. But such an approach was not attractive to self indulgent parliamentarians, woefully ignorant about the real problems of economic development, who wanted to be able to demonstrate quick aid results to their constituents. Because most countries were *dirigiste*, their growth was slow and poverty prevailed. Aid fatigue hence threatened the national and international aid establishments. In response, a messianic approach to development began to distort analysis, promising a short cut to development by relieving poverty directly.

The World Bank's change of direction had some positive aspects. In *dirigiste* economies irrigation projects often failed to dig the canals to bring water to farmers. In the absence of the measurement and charges for irrigation water flows, much water was wasted and the benefits went to large farmers. There were other linkages to market orientation. But the shift of analytical endeavour toward "grass roots" development did not lead to poverty alleviation. Measures to stimulate rural development by extension services instead of investment in rural infrastructure, feeding programs for small children and pregnant women, micro finance for poor women (the men knew better than to repay loans), did not have permanent

growth effects. Most of the rural development projects in sub-Saharan Africa failed to achieve their targets (Léle 1990). Only in the framework of overall liberal economic policies, as in Thailand and Indonesia, for example, were rural poverty alleviation programmes effective. In such circumstances they did not require foreign exchange inputs. They could be undertaken effectively by governments for whom poverty alleviation was a priority and were not effective where this was not the case. Foreign aid involvement usually hindered grass roots programmes. But turning to direct poverty alleviation gave the World Bank new allies in NGO pressure groups. By the late 1990s they have come to dominate James Wolfensohn's agenda at the cost of attention to growth and development.

With direct poverty alleviation claiming the bulk of staff attention, the Bank failed to discern the developing countries' expansion of borrowing in petroleum rich international capital markets. When the most distorted economies, with the worst macroeconomic policies, were the principal culprits, the debt "crisis" hit the World Bank in the jugular. Developing countries ceased to be able to, and sometimes to want to, borrow, particularly for foreign exchange components of projects for which they did not want to use complementary domestic funds. Liquid international capital markets, in any case, made World Bank intermediation superfluous. Although high debt servicing levels were a symptom of macroeconomic collapse following years of domestic economic mismanagement, the debt "crises" of the late 1970s and early 1980s were presented by the World Bank as the result of external shocks caused by inter-

national capital markets and subsequent trade fluctuations. The very necessary policies adopted to curb inflation in industrial countries after price blowouts in the 1970s, were blamed for the developing countries' difficulties in the 1980s. The World Bank found a way out. With little difficulty at the Board level, the Bank introduced "programme lending" so that the difficulties of project lending could be replaced by writing much larger cheques for governments whose irresponsible policies had resulted in national bankruptcy. Any conditionality that was written into such loans depended on policy reforms that could only become effective over years of policy reform. Such analysis as was undertaken for so called "adjustment programme" loans (charmingly labelled SALs) clearly indicated that the problems that required policy adjustment were caused by domestic policies not by international economic trends or events. Such analysis was ignored as a new wave of "adjustment economics" codified policy issues into the "Washington consensus" (Williamson 1994).

By the late 1980s "adjustment" had run out of steam. Poverty alleviation policies, though still very popular with naive industrial country politicians and NGOs that accessed increasing government subsidies by pandering to them, were clearly ineffectual in practice. And a new factor emerged in the international aid industry. Japan was becoming the leading aid donor. Japanese bureaucrats sought support for the "Japan Inc." model of development from developing countries and international institutions accepting their aid funding. The World Bank lurched into yet another analytical initiative to maintain its lending programme. Japanese fund-

ing was provided for a major "research" project that would support the "Japan Inc." model. Although the resulting *East Asian Miracle* (1983) was deeply flawed, it was published under the World Bank's arrangement with Oxford University Press, and strongly promoted by the Bank's public relations machine. Development practitioners were told that there was nothing wrong with Japanese *dirigiste* economic policies just as Japan fell into a decade of recession.

It had been clear from the late 1970s when the demand for Bank funding was falling, that the World Bank was over-staffed for the tasks it was performing. "Platinum" handshakes became a major budget cost, funded, of course, out of the service charges to developing country borrowers. The quality of its analytical work had declined in spite of staff expansion because of the Bank's working style. World Bank staff worked hard, often 60 hours a week or more and they travelled incessantly in the attempt to complete ever-increasing lending programmes. Resident offices were established in large developing countries and in groups of countries to push the completion of lending programmes. The World Bank, like the IMF, failed to draw on the rapidly emerging analytical skills of developing countries. Twists and turns of analytical theory and practice followed the needs of the institution not of development countries. Economic and other reports did not increase their use of local resources. The Bank's large technical and research establishment talked to itself, freezing out analytical questioning, let alone opposition in the meetings and conferences constantly being

organized. Fortunately, as the relevance of the Bank's contribution to economic development was becoming questioned, the centrally planned economies collapsed creating a large new borrowing clientele first in China and then in Eastern Europe. These countries were not "borrowed up" and few of the "transitional" governments found the "Japan Inc." model unpalatable.

The World Bank introduced loan evaluation, creating a separate entity in Operations Evaluation, that, correctly, formally did not report to the management but to the Board. Initially project evaluations were merely accounting audits that sought to find out whether loan funds had been spent as intended. Most of the evaluations were accordingly positive. In this limited sense the World Bank was cost effective. But these evaluations did not ask whether the project and programme loans had been efficient and effective in promoting development. In the 1970s, although the World Bank was extremely reluctant to undertake evaluations of its contribution to development as part of its research programme, broader examinations of its efficiency and effectiveness, were undertaken by the Operations Evaluation unit. The evaluations, though voluminous, were not very rigorous. They confirmed that the key factors in overall development and in project effectiveness were the borrowing countries' domestic policies and the effectiveness of their institutions. The World Bank's contributions to a country's development were small except in the early years in small countries. In terms of its contribution to policy orientation, it appears that while its influence was negligible in its early years,

it was probably positive in the 1960s and 1970s until messianic imperatives overtook analytical endeavours. The endorsement of the Japan Inc. model reduced the effectiveness of long term growth analysis further. Thus, in spite of the numbers of staff working on East Asia in the region and in Washington, the Bank failed to discern the costs that crony capitalism was about to impose on the region. With all the attention to poverty, the effect of the currency and financial crises on the livelihood of the lower income sections of the population were not foreseen, and when finally examined, were not convincingly analysed. In the guise of relieving poverty, the Bank appeared to be mainly concerned to ensure that international and national funds would rescue the cronies who had caused the problems.

Bank staff were originally recruited from colonial administrations, banking institutions and capital markets and specialized private sector firms in relevant disciplines. Over time the World Bank experience became an important training ground for development professionals, particularly for developing countries. Staff turnover was reasonably high with many staff members returning to their own countries. Remuneration, arranged together with the IMF, was high enough, together with the Bank's professional reputation to attract high calibre professionals, but the abandonment of critical analysis undermined staff quality. World Bank officials are seduced by their ability to mix on equal, or, if the loan and lending programme, are large, on more than equal terms with heads of departments and ministers. In developing countries

staff members, particularly if resident, are constantly exposed to the company of the country's leading technocrats and politicians with whom they spend their leisure as well as their working lives. Their children are isolated in schools for the children of the top brass and other international mandarins. Few have been able to find their way to local academic, let alone broader circles. The World Bank's recent move to shift responsibility for lending from Washington to resident offices has ended what little conditionality remained. The independence engendered by professional technical reviews and inputs in Washington has disappeared. Heads of World Bank missions are inevitably suborned by local officials. National and international cronies can now deal together in comfort.

Many of the best performers have left the Bank. While it has been, and still is, possible for professionals at middle and junior levels to devote themselves to tasks that do no harm to developing countries, the twists and turns of policy have made this impossible for senior staff. Questions of what the countries that own the Bank, not least the developing countries that pay for its operations should do about it, have become acute.

Concluding Notes

The low rates of growth of the majority of developing countries during 50 years of IMF's and World Bank's activities suggest that overall, though they may have had some effect in mitigating *dirigiste* policies until the 1980s, they have not been effective. Their failure to anticipate the East Asian "crisis" and

their subsequent failure to advocate fundamental reforms suggests that they no longer play a useful role in the international economy. China and Vietnam continue to avoid financial "crisis" by not having financial sectors. The growth figures reported for these countries by the IMF and the World Bank clearly do not reflect reality. Continuing support for counterproductive national policies, contributing to moral hazard and attempting to create new international capital market institutions do not inspire confidence. It is moot whether international assistance can help sub-Saharan African or transitional economies. It does not seem to have been effective to date. Both the IMF and the World Bank appear to have passed their "use by date". The liberalization of trade and capital flows that they successfully urged in their early days have made them redundant.

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Indonesia and the Military at the Crossroads

Rowena G. Layador

Introduction

INDONESIA'S military has been entangled in the nation's political, social, and economic affairs through *dwifungsi* or dual function. Their role has been considered to be a hindrance to the introduction of democracy and reforms. Born during the shackles of the independence struggle, they became the most cohesive institution and subsequently used by Soeharto for his political ends and ceased to be the armed forces of the nation state but just the state. With Soeharto's resignation, they came under the scrutiny of the people that demanded an end, or for the moderates, a reduced role in politics. The transition is crucial to the country's prelude to democracy but the process is just embarking.

The explosion of political expression in May 1998 paved the way for Soeharto's resignation, the New Order finally delegitimized after 32 years. The subsequent events after May 1998 seem to have created a pretext for the military's increased role yet the great euphoria created new expectation and that is: political transition from authoritarian to democracy. In creating a more democratic society, it has to address numerous issues. Political devel-

opments since Soeharto's resignation rest on the following issues: (1) the need for the leadership to seek fresh mandate through a free and fair elections; (2) expansion of political participation and sustaining civil society's vigilance; (3) arising problems of national disintegration; and, (4) questions on the new role the military will play in the current political climate.

The deepening economic crisis precipitated the escalation of mass protests and greater demands for political reform. The value of the rupiah has fallen more than 50 per cent against the dollar, prices have gone up, company closing consequently leading to increased unemployment; and it was predicted that the "per capita income in Indonesia would tumble as low as \$750 from \$1200. That means that the number of people classified as absolute poor could swell from 24 million to 42 million or one out of five Indonesians."¹ Hal Hill would describe the economic downturn in Indonesia as "strange sudden death of a tiger." However, its sudden death created social and political unrest that led to the resurgence of demands for greater democratization.

The successive outbreaks of violence from 1997 to 1998 were a form of political

resistance to a government that is perceived as ineffective, politically corrupt, and inept in addressing the worsening economic disparity. The economic crisis has indeed ignited democratic aspirations, and the source of legitimacy ceased to exist as economic hardships mount. Observers say that without the collapse of the economy, which formed the base of President Soeharto's legitimacy, there would not have been the opportunity for political change.²

Though there was a change in leadership, the same regime still exists. Some quarters argue using the term Post-Soeharto in the discourse since it is not yet Post, rather the same old cake with a new figure on top. Moreover, Habibie is just a continuation of Soeharto regime without Soeharto.³ In Indonesia, the first order of business is to restore political order before political change can take place.⁴ The task of this paper is to identify the salient issues of political development in Indonesia after Soeharto and how issues of economic decline and national integration can affect transition. Moreover, whether there is indeed a military resolve to disengage in politics in spite of pressing domestic problems.

Channels or mechanisms that provide for citizen mobilization and allowing them to speak out their political/social grievances are imperative. The role of leadership and restoring political authority is a prerequisite in establishing political/social order and change. Moreover, the leadership needs legitimacy currency to implement reforms and changes. In this case, the general election in June 1999 was a step towards putting the house

in order and national integration and unity as primary to Indonesia's political goals which implies mending political fences. Another is the military. Will they allow democracy to transcend in Indonesia or will they prematurely terminate the process in the name of preserving the unity of the nation? However, it should be noted that the military is viewed negatively by the public for their repressive ways and human rights violations committed in accomplishing their internal security task. There is a need for them to undergo image building in order to make their institution credible to the public eyes.

Indonesia is a multi-ethnic society, divided along ethnic and religious lines coupled with aspirations of independence. Violence in Aceh, Irian Jaya, Madura, East Timor and Ambon are lingering political problems of this nature. Riots have occurred in the past and were directed against a particular ethnic or religious group. The task of whoever will lead Indonesia in the next millenium is to reconcile these forces, but a legitimate leadership had to be earned first. Threading together a highly divided nation is an enormous task.

To emphasize the legitimacy variable, Myron Weiner stressed the importance the concept plays in solving problems of national integration.⁵ Though, President Habibie's efforts to reach out to the parties, e.g referendum for the Acehnese, and political solution to East Timor, are necessary first steps at this point in Indonesia's history. Nevertheless, he has to earn the acceptance of the people of his leadership. In this view, the national elections is a crucial first step along with the proliferat-

ion of independent political parties ending the political dominance of the state party *Golongan Karya (GOLKAR)*. Should the new leaders fail in this regard, political disintegration is a possibility that may lead to military intervention.

As part of nation building, establishing national unity -- unity not in geographical terms rather a feeling of being part of one nation is very important. Ethno-national concern in some parts of the country is one of the military's justifications for its continued role in internal security. Though, solutions are primarily political in nature and not military.

Separating the military from politics is one big challenge. A noted scholar said that military intervention is an inseparable part of political modernization, and this has been proven several times in history.⁶ In Indonesia, the Armed Forces have been a major actor in the political front as part of *dwifungsi* or dual function linking their role to politics. The road to transition is not easy to traverse. The Philippines for its part has experienced its own difficulties and political pain.⁷ When former President Aquino assumed office in 1986 ending 20 years of dictatorship, she was confronted with problems of economic dislocation, a politically divided society, and a highly politicized military.

Will the military create a relationship where they are subordinated to civilian institutions? What are their roles in the current political framework? Will they go back to the barracks? Is there a desire to withdraw from politics? What are the reforms they have undertaken in response

to public demands and to clean up their discredited image. It is foremost that the armed forces support the demands for greater democratization since their support or non-support will certainly have an implication for Indonesia's political landscape.

Issues of Political Development in Indonesia

Soeharto left the country in a politically chaotic situation occurring in conjunction with the economic crisis or *krismon*. The "severe economic crisis has also made the people aware of the ossification of the political system, for more than three decades manipulated to maintain the increasingly absolute power of the New Order Regime at the expense of the people."⁸ Though enjoying a remarkable political space, a weak government had to face a sudden political implosion and resurgence of civil society. They demanded greater democratization, but at the same time, there is increasing civil disorder as exemplified by continuing violence and riots, blossoming of separatist movements and ethno-national concerns, and a politically battered and discredited army whose image needs an overhauling. The primacy of reforms are urgent tasks to enable the state to cope with these changes prompting President B.J. Habibie to initiate political reforms.

The old political framework according to Soeharto's successor "was no longer adequate to respond to the demands and aspirations of the people."⁹ Holding together a multi-ethnic nation under these chaotic conditions, bring to fore the is-

sue of legitimacy and political authority and the challenge on how to transform Indonesia into a more democratic society.

Leadership under Fire

Habibie's leadership is perceived as an extension of Soeharto's regime, thus, the "Post-Soeharto" term is a misnomer. His assumption to the highest position lacked political legitimacy to credibly lead Indonesia and carry out political reforms. Even Soeharto and the military initially doubted his capabilities to lead and civil society themselves rejected his regime. It was a leadership constantly under suspicion, scrutiny, and skepticism by the Indonesian polity. There was very low political confidence and that "there was little doubt that he came to power at a most inauspicious moment in Indonesian history."¹⁰

To meet challenges in the current era, it has to allow people a greater say in government and at the same time institute reforms that would improve his legitimacy and thread societal cleavages lest sink into deeper crisis of legitimacy. The imperative of gaining consent is a currency that will enable him to pursue needed reforms towards democracy. Dan Quart Rustow said, "restoring governmental authority is needed in political development." Initial steps he undertook to improve on his credibility is to call for general elections in early 1999 and revoked restrictions on number of political parties and on freedom of expression, association, and assembly. Even his announced plan for a general elections has been viewed with doubt that the gov-

ernment might delay the June elections citing technical and administrative difficulties such as registration, ID, and so forth.

As part of the initial step, several political laws were amended including, the composition of the House of Representative (DPR) and the People's Consultative Assembly (MPR). Formal discussions on political laws were opened to the public for inputs making the process participatory, thereby, dismissing suspicions that the government is manipulating the amendments of political laws to its advantage. Changes include reduction of military (ABRI) representatives from 75 to 38, restrictions on political parties no longer exists, thus breaking Golkar's political dominance. Currently there were about 48 parties participating in the June elections. As part of the electoral reform, an independent General Elections Commission (KPU) was established. The KPU was composed of representatives from government and political parties. Furthermore, civil servants are prohibited from joining political parties. The latter, implicitly implies state's determination to make the bureaucracy appear non-partisan and therefore does not have to support Golkar, the state party.¹¹

In addition to political laws, Habibie released political detainees and prisoners on a conditional basis. In doing so, he attempted to pay particular attention to the promotion of human rights. It has also allowed the formation of labor unions, thus increasing the participation of civil society. The DPR passed the Clean Governance Bill that will increase the ac-

countability of public servants specifically government officials. The Bill requires them to declare their assets when they begin and end their tenure with the state.¹² It is an effort to make the bureaucracy more palatable to the public, at the same time, increase accountability.

One key demand that has to be addressed is the investigation on the wealth of Soeharto. Although he has ordered the Attorney General to look into the charges of alleged corruption, collusion, and nepotism by Soeharto, expressions of "doubts by some political observers on the seriousness of the government's investigation are quite evident."¹³ No tangible result can be seen on this issue and until now the people still wait.

In spite of the reforms, Habibie suffers from low credibility and confidence. He is to some retired military officers as "a symbol of the corrupt and repressive new order," and his nomination by Golkar as its presidential candidate was described as "death knell of the current reform movement."¹⁴ Political analysts say that Megawati and Amien Rais is even more popular than Habibie.

The June 1999 Elections: A First Step

President Habibie's announcement of an early election provided a douse on his seat. Publicly stating that it would be better even if only 30 per cent of voters came or whatever number so long as it be held honestly, justly, democratically, and open. Moreover, it is preferable to have free and fair elections than a 100 per cent turn out in a fraudulent poll.¹⁵

The general election is a necessary first step to enable government to proceed with a firmly intact legitimacy to draw upon. "Though not a panacea," according to political scientist Mochtar Pabottingi, but would at least bring the nation to the gate of true reform.¹⁶ It is a make or break situation and the only alternative; thus, ensuring the success of the election is important. Political order had to be restored, government recognized so that reforms can take its course.

However, the recurring violence in some parts of Indonesia may derail the elections including prospects of using coercion and money politics to influence the electoral choice of the people as well as its outcome. In sum, the democratization process is in the offing. Some possible worst case scenario have been identified by Samsu Rizal Panggabean:

1. Incompatibility between old, anti-reform coalition and pro-reform movement over the new rules of the game. This will increase fragmentation in society;
2. Flawed election;
3. Failed election due to widespread riots and social upheaval in many places that would make the election impossible to organize;
4. A winner-takes-all attitude among political parties. A dangerous attitude that exclude many elements of the Indonesian society. An inclusive political attitude would be more desirable especially in an interregnum period.¹⁷

Most reforms to be instituted are dependent on this electoral exercise and

there is no room for failure. It is a "jury for setting political differences and putting in place a legitimate government to run Indonesia in the next five years."¹⁸ Nevertheless, the democratic future is still uncertain and the possibility of sliding to political upheaval is not remote. Though the opposition, specifically the party of Megawati Soekarnoputri, won the initial battle, the problem of making everyone work for democracy is an enormous political task that should not be ignored by the present leadership.

Threading a Nation

Aside from Indonesia's multi-ethnic composition, the transmigration policy of Soeharto has been blamed for the current national disintegration problem. It is also important to note that the economic inequality felt by those resource-rich provinces is another factor to consider. Military option has been the instrument of the state in suppressing independence aspirations in Aceh, Irian Jaya and East Timor. The military option added to the resentment of the locals to Jakarta. As a consequence human rights abuses were committed by the military contributing to feelings of social injustice.

The government made extended efforts to unruffle the issue. One such effort is General Wiranto's apology in 1998 following Habibie's in Aceh, as a way of appeasing the province.¹⁹ Yet, the people's sentiment remains. A scholar noted that some of the most widespread political movements during the past decade were not organized around class, or on economic issues, but rather centered on religion or ethnicity.²⁰ Indonesia seems to

fit this description. It has been beset by both religious and ethnic disturbances which became more pronounced when Soeharto resigned in May 1998.

In the hope of ending the lingering political conflict in East Timor, President B.J. Habibie announced an autonomy package for East Timor. This package will allow them to manage their own affairs, except foreign policy, external defense, and monetary matters. Should the Timorese reject autonomy through referendum under the auspices of the United Nations, then independence will be given to them. Though political solutions are at hand, greater political disaster is in the offing as society became divided on the issue of integration and independence.²¹ This political decision is "an acknowledgment that the government has failed in its attempt to integrate East Timor into the nation."²²

The only solution that Habibie could offer is to pass political fate of the province to the next People's Consultative Assembly. Violence has been escalating between the separatists and the military. The Indonesian flag was replaced with an Aceh flag. It is also an indication that the situation may escalate into a less manageable level. This means that the resolution to Aceh has to wait until after the June elections, making the exercise more crucial than ever in this regard. At the same time, the current government is washing its hands by making the next MPR the responsible institution to draw up political solution.

In Irian Jaya, Robin Osborne's assessment of the situation in the 1980s is that the resistance movement will not abate.

For over 30 years since its incorporation in Indonesia, the West New Guinea is more reluctant than ever to live under what they consider as "foreign rule."²³ The feeling of exploitation is still the prevailing sentiment and they feel that what "they (Indonesia) want is our land, not our people."²⁴ In April 1999, leaders in Irian Jaya have expressed their desire to be masters of their own land.

Problems in Irian Jaya, Aceh and East Timor are yet to see the light of the day. Nevertheless, these problems cannot be solved in matter of year. Above all the psychological baggage which include political pain and frustrations will probably take generations to heal.

Sectarian clashes in Ambon and ethnic violence between the Dayaks and Madurese in West Kalimantan have only exacerbated the government's political-social concerns on the one hand, the separatists movement and religious and ethnic clashes on the other. In Ambon, it is not only about sectarian violence, they also seek to breakaway from Indonesia and establish the Republic of Moluccas. Restoring civil order is primary, as anarchy and savagery are committed as exemplified by the head hunters enterprise of the Dayaks.²⁵ As violence escalates, the number of politically displaced people will increase. In Maluku alone, 25,000 people have fled their homes and 300 people have been killed since January 1999.²⁶ This phenomenon will lead to economic displacement, with the economic crisis as the backdrop.

The Chinese exodus in 1998 is a phenomenon that deserved appropriate attention. As scapegoats for the economic

woes that the country is experiencing, the Chinese became targets of riots and violence. Their exclusion from society emanated not because of their racial affinity rather because of their economic success. Most observers assessed that it was not the primordial factor that triggered riots and violence against the Chinese but rather economic. This observation was also affirmed by Jamie Mackie that antagonism is undoubtedly because of their economic dominance and exclusivism, holding approximately 70 per cent of Indonesia's corporate wealth while they only constitute 3 per cent of the population.²⁷ Moreover, it is also related to the problem of social and legal injustice and feelings of disadvantaged and underprivileged aside from gross wealth disparity.²⁸ This situation created a social discord and the Chinese integration into society will be a long process.

Organizing Through Decentralization and Autonomy

In this regard, Indonesia has to think of another way of organizing society and resolving gross wealth disparity. Threading society falls within the discourse of decentralization and autonomy. Federalism has been advocated by some quarters as a corrective measure in the *reformasi* era. To some non-Javanese leaders, autonomy including a heftier share of locally generated revenues that now go to Jakarta will help to quench resentment that has fuelled sporadic rebellions.²⁹ The House of Representatives (DPR) recently passed a Bill that provides autonomy to regional administrations and legislatures from the Central Government.³⁰ A Bill on profit sharing has been passed likewise in

April. The bill "stipulates that earnings from the forestry, general mining, and fishery sectors will go to the provincial governments with the central government receiving the remainder." For example in oil, Jakarta gets 85 per cent and the province 15 per cent.³¹ These bills passed at the most tumultuous moment in Indonesia are a foot forward toward lessening the social strain that threatens to break the Republic. The integration of the Chinese will surely take a long time to achieve so long as the gap between the rich and the poor persists.

The politicization of religion may in fact unsettle the balance. With the rise of Islamic parties, some sectors more specifically the ABRI, are actually wary of this development should the formation lead to religious exclusivism. The ABRI is historically not fond of this idea and used Pancasila against formation of Islamic parties.³²

The state finally responding incrementally to calls of change, and reforms is besieged not just by economic woes, but as well as the perennial dilemma on how to weave the Indonesian society. What keeps the state on their toes is the continuing vigilance of civil society.

Resurgence of Civil Society: Keeping the Torch Alive

Civil society has spoken with the students as the leading actors. After more than 30 years, shackles of the state were finally broken. The students with the support of civil society forced Soeharto to resign in May 1998. The unabated demonstration that started in February 1998 sus-

tained the reform movement leading to the May historic event that consequently opened the floodgates of greater democratization. It was reminiscent of the 1966 student activism that brought Soekarno down. But their success in 1998 was largely attributed to the economic pinch felt by all sectors of society. Moreover, this time no military took the center stage.

The student movement is divided into two groups: the radical and the moderate. The first advocates changing of existing regime and set up a transitional government while the latter believed in the gradual process of reformation. They see the June 1999 elections as an initial step. Based on what is happening in Indonesia, the moderates seem to have won the day.

The cleavage is not too wide to affect their over-all desire for political change. On the one hand one wants to participate in the process either ensuring a fair and free elections or by keeping the issues under government's constant attention. The University Network for a Fair and Free Elections (UNFREL) is one such organization specifically established to monitor the elections. On the other, the radical group keeps the issues alive yet more confrontational and more radical. Still violence persists in student political expression. One recent news reported that students were forcing their way into the state radio station in Bandung resulting to injuries. The students wanted to broadcast their concern over the latest social and political developments in the country.³³ This connotes that in spite of political openness that ushered in Indonesia, there is still limited avenue or democratic space for airing their concerns.

The total abolition of the military in parliament is one of the rallying issues of the students. Yet this democratic space that civil society is enjoying was allowed to flourish by the holders of the instrument of coercion -- the military or the *Tentara Nasional Indonesia* (TNI). Their role in society for 32 years has been one of the contentious issues in the *reformasi* era. However, it is also important that with its resurgence, and for democracy to have meaning, political observer Jusuf Wanandi emphasizes the concomitant guarantee of political rights of civil society.³⁴

As for other societal forces, though NGOs have played a significant role in Indonesia's socio-political scene, they have yet to establish its mark. Workers are getting more organized and has put forth issues such as wages, prices of commodities and even the government's social safety net program.

Going Back to the Barracks?

The TNI introduced as a new prominent political player in 1967 is now being asked to reduce, if not, totally stay out of politics. The institution is currently facing the biggest challenge since their inception. Asked to go back to the barracks, facing ethnic disharmony, outbreaks of riots and violence and independence aspirations and at the same time re-organize itself at this moment in Indonesia's history. As pivotal player in Indonesian politics for 32 years, is the military ready to take a back seat?

The military establishment now open to public scrutiny has been subjected to criticisms because of the role they

played in perpetuating Soeharto's dominance for more than 3 decades. The issue of gradually shedding their participation in politics and the clamor to go back to the barracks continually besieged the institution. It has no choice at the moment but let democracy flow, and hopefully let it flourish and mature eventually. Yet there are still apprehensions about the kind of role they envision themselves to be. Do they intend to go back to the barracks? Will the current political constellation compel them to abstract their role?

The issues discussed in the preceding pages emphasized the importance of the electoral exercise in June 1999, the utmost need to re-organize society as imperative in weaving the nation together, and the sustaining torch of civil society. In the past its political interference was most often conducted through repressive rather than persuasive means.³⁵ Its image heavily tarnished after Soeharto's resignation has to reform itself and declare a clear vision of what they want to become. The military is not yet ready to fade out of the political sphere just yet.

The succeeding section will focus on TNI's inception and the justification used that allowed them a pervasive political presence in society. Civil-military relations in Indonesia will certainly spell out the success of reforms as well the goal of democratization.

The Tentara Nasional Indonesia (TNI) in Retrospect

For 32 years, the Indonesian military has been a major political player. Most literature dealing with the Indonesian mil-

itary are in agreement that the government did not form the institution but was born out of the independence struggle -- it was a national liberation army.

What facilitated its dominance in the last three decades in the political, economic and social spheres of the Indonesian society can be attributed to several factors. Factors such as its role in the independence struggle, the self-perception as savior of the nation, and the weakness of the civilian leaders to govern since the creation of the Republic of Indonesia. Ulf Sundhaussen described the latter as a systemic failure, a factor that will compel the military establishment to assert itself in politics.³⁶ What facilitated its preponderance will certainly bring us back in the early years of the Republic. From an Armed Forces of the nation-state, they became an instrument by the state to maintain itself, more specifically to perpetuate Soeharto's reign in power.

At the Onset

Even at its inception, much of its organization is not attributed to civilian political direction. By the time the armed forces were officially formed in 5 October 1945, they had established ethos of independence of government.³⁷ Moreover, it was established prior to the creation of the Republic of Indonesia.³⁸

J. Kristiadi would illustrate their history by quoting Salim Said:

It was a self-created army in the sense that it was established neither by the government nor by a political party. Instead, the military created, armed and organized itself out of the shambles of the Japanese trained Indonesian militia following the

surrender of the Japanese and the proclamation of independence in 1945, when the newly created-organized government was reluctant to raise an army.³⁹

The reluctance of creating the army for independence struggle emanated from Soekarno's apprehension of antagonizing his allies and prefers to achieve independence peacefully. The youth then took the initiative to arm themselves and defend the country.⁴⁰ Thus at the beginning there was a seeming institutional independence from the civilian institution or worst without civilian direction. Initial dynamics of the civilian and the military would latter on have implications in the ensuing years, which helped shaped the civil military relations. This self-creation characteristic would serve as one of the justification of its involvement in politics.

Setting the Stage

The political assertiveness of the military is based on its defining historical experience, events that made civilians ineffective, which became formalized through various doctrines. One assertion is history. They carried out the resistance leading to Indonesia's attainment of independence. According to Robert Lowry, its political preeminence is based on its central role in the independence struggle. They kept the struggle alive while the Soekarno was perceived to have abandoned it.⁴¹ Most Indonesian scholars would conclude that from that time on, the government lost its opportunity to control the armed forces.

Aside from their historical role, the institution developed from bottom to top. This means that it was the military

themselves who developed the institution. At the initial stage, the organization of the armed forces showed the central government's lack of authority. This is exemplified even in the selection of the commanders. Dr. A.H. Nasution who was appointed West Java's command chief of staff was unable to select his own commanders, instead he found himself confirming existing commanders.⁴²

At the same time, the reorganization of the defense establishment was not decreed by the government, the senior officer corps ratified it.⁴³ The military's early experiences in governance can be traced during the independence struggle, when the government was unable to direct them. At the height of the guerilla war, they set-up parallel civilian government apparatus. Salim Said would ascribe this situation as a contributory factor to the military's early taste of civilian governance.

The self-perception of its self-creation remained and written down in the military's annals of history. In the military's perception it was their effort that ultimately brought about recognition of its independence by the Dutch.⁴⁴ Consequently they see themselves as a vital actor in the socio-political affairs. The army's assertiveness is seen through General Sudirman, the *panglima besar*, opposition to government policies that affects the army. Such policies include the 1948 Rationalization agreement with the Dutch, which demoted Sudirman under the defense minister. Opposition did not emanate from the policy itself but its context, which pictured the armed forces as weak and unprepared for the struggle.⁴⁵ The first major political crisis in-

volving the army was the 17th October Affair in 1952 where the army requested Soekarno to dissolve the Parliament. This action emanated from the seeming overarching actions of civilian political leadership in military internal affairs. Former officers of the PETA officers resisted the rationalization and demobilization plans by the Dutch trained officers of Jakarta and Bandung.⁴⁶ This is just one of the series of the army's assertions of its opinions and views on government policies. Looking back, more often than not, history's interpretation can be very subjective, as it is open for various explanations, renditions may lead to omissions. Robert Lowry would attribute the success of the struggle to both diplomatic and military efforts. There seems to be non-recognition of the civilian political leadership in making political decisions that contributed to the success of the struggle.

The second assertion rests on the numerous operations the military conducted against outbreaks of rebellions in the outer islands (outside Java) and dissent within the army years after attaining independence. This indicated a factional conflict within the army that culminated into rebellion and set up the Revolutionary Government of the Republic of Indonesia (PRRI). The army was called upon to quell these revolts and rebellions. The various uprisings were interpreted largely as having been caused by the inability of party politicians to solve the latent problems, as well as a result of the political experiment after independence.⁴⁷ The military at this stage is starting to be a reactive institution that

will later on demand a more active role in non-military affairs. After the anti-rebel and PRRI operations, the army was all the more determined to concentrate on putting law and discipline in order, and cleaning up the state's organization both civil and military.⁴⁸

As soon as the period of Guided Democracy was ushered, the army became politically assertive, entering into an even higher stage of participation. This participation was facilitated by Martial Law. Numerous anti-rebel operations, reinforced the army's conviction that military campaign alone, without accompanying political and economic measures would not provide lasting solutions.⁴⁹ Thus, a say of the army in non-military affairs appeared to be essential for maintaining the country's external defense and internal security capacities.

Hence, the Middle Way concept was conceived in co-operation with the civilian government. "It is the middle way doctrine that launches the formal departure on the long journey of the *dwifungsi* (dual function)."⁵⁰ With the blessing of the civilian authorities, the military's entry into the political, economic, and social spheres was made legal. This concept gives wide opportunities for participation of the military outside the fields of defense. To illustrate their say in the politics, as early as the late 1950s, the military proposed the return to the 1945 Constitution after the 1950 Constitutions failed to consolidate Indonesia. Moreover, aside from the return to the 1945 Constitution, the military also proposed the reduction of the number of parties and introduced functional groups in the political

system.⁵¹ Other proposals were civil servants and the armed force and police are prohibited from joining political parties and soldiers do not exercise the right to vote. In return, members of the armed forces should be appointed to parliament and constitute one functional group.⁵² And to borrow Samuel P. Huntington's term, ABRI became the soldier reformers and performing a dual function -- the military and non-military functions.⁵³

The turbulent years in the late 1950s and until the 1960s led the military to take-over in 1967. There is increasing systemic failure -- widespread lawlessness and increasing rebellion, riots, demonstrations and violent clashes in some parts of the country. This political backdrop was coupled with economic decline.⁵⁴ At the same time in 1955, the general elections failed to resolve the causes of political deadlock. This was the time when the communists were supposedly staging a coup in 1965 that was quelled by the military after summary executions of both suspected and self-professed communists.

Adam Schwarz would rationalize the military's ascendancy emanating from experiences with Parliamentary Democracy that convinced the army that the country needs a stronger government.⁵⁵ A strong state relatively insulated from the interests of any particular group and capable of suppressing antagonisms based on ethnicity, religion, or geography. Thus Soekarno was no longer a viable leader and unable to lead the country out of chaos and making the military the only institution that can hold the nation together. Therefore, they are not only the unifier or *pemersatu* of the country, but as well as the savior or

penyelamat of Indonesia. It is also important to note "that their experience in non-military activities before 1965 had shaped a political style more suited to the advancement of officers' interests within the existing structure than to the creation of an entirely new political order."⁵⁶ At the same time, officers started to refer to their experiences in with civilian politicians during and after the revolution.⁵⁷

The Doctrines

According to Harold Crouch, the expansion of the military's political role was not a planned process rather took the form of a series of responses to particular crises arising, in the main, from actions of dissident officers. This opportunities were formalized into Major Abdul Harris Nasution's Middle Way concept that described the military's purpose as two-fold: a military force as well as a social-political force. This entailed their representation in the Cabinet, civil service, and the parliament. This doctrine latter on expanded to *Dwi-fungsi*, that explicitly rejects any notion of a strictly apolitical stance and asserts its rights as savior of the state and defender of the Pancasila to justify a permanent role in society.⁵⁸

After the political upheaval in 1965, Soekarno and the communist party were thrown out of the political limelight and the military emerged as the major political actor.⁵⁹ As the New Order of Soeharto, the expansion of the concept began. This provided the theoretical backing for the military to expand influence throughout the government apparatus -- the military's role was to become permanent.⁶⁰ The creation of GOLKAR, the state party, paved the way

for the military to constitutionally justify its growing political influence. Shwarz would quote David Reeve's rationalization of these changes as:

If the nation were conceived of as made up of Golkar, and the Armed Forces were included among them, the military were entitled to play a role in all fields, political, economic, as other Golkar did.⁶¹

One observer also shared this observation, as the military's way of legitimizing participation in Indonesia's political life. In the New Order era, the military is given 20 per cent of the seats in the DPR or the House of Representatives. Some seconded personnel are posted to jobs ranging from Cabinet Minister and departmental secretary-general, to village head, and directors of government enterprises.⁶²

Other legitimizing doctrines are found in the Doctrine of National Defense and Security, and the Doctrine of Non-Military Function. The former stipulates the consolidation of the national core through national resilience. This is also contained in the *Wawasan Nusantara* or Archipelagic Outlook, which insisted on the geographical and social unity of the nation.⁶³ Thus, explains the military's overarching presence in the countryside to address or dilute primordial affinity since the country is an ethnically fragmented society. Moreover, their internal security doctrine assumes that there is an ever-present actual or latent threat and that society therefore be managed and developed to strengthen its internal resistance, cohesion, and capacity to meet challenges.⁶⁴

The second doctrine is a fulfillment of the National Aim as stipulated in the Pre-

amble of the Constitution. According to Soeharto in 1971, the mission of the Armed Forces in its Non-Military function is to participate in every effort and activity of the People in the field of ideology, politics, economics, and the socio-cultural field.⁶⁵

ABRI doctrines stressed that the Armed Forces politics is the politics of the nation, not of the government. To ensure national interests are upheld, ABRI must therefore play a role in the law making and government.⁶⁶ With the army's representation in the Parliament, civil service and even the economy, they became the dominant actor in the New Order Era.

The military emerged as major actor in politics through the historical processes that reached its fullest expression in 1967 that will continue 32 years latter and counting.

An Economic Actor

"We make profits to meet the non-budgetary expenses of the ABRI (TNI)."⁶⁷ This is how the army rationalizes its role in the economic sphere in order to support their meager budget and routine needs. Moreover, ABRI business ventures help boost funds for defense, and at the same time give members less visible sources of extra income.⁶⁸ Aside from that, their involvement in business also rests on the following rationale: (1) to support their dual function; since national development is a shared responsibility; (2) housing for troops or welfare funds for the troops; and (3) that it contributes to capital formation and development of business skills.

Lowry traces their business history since the revolution and the main purpose was to support its militia units. However it was in 1957 when they began to run large-scale commercial enterprises as soon as the Dutch businesses were nationalized. The corporate wealth of the Armed Forces is estimated at US\$8 billion⁶⁹ whose empire extends from pulp and paper, logging, franchises, ferrying cargo, crude oil refinery to management of state enterprises such as the state oil company *Pertamina* and *Bulog*.

Though its business provides additional income to the establishment, the people heavily criticized it. Critics say that the ABRI should retreat from civilian functions like running the enterprises and even some officers also believe that the armed forces have no business being in business.⁷⁰ At the same time, it has affected their efficiency, because many troops effectively hold two occupations -- soldiering and seeking to augment their base incomes either collectively or individually.⁷¹

Well-Entrenched Military

Its historical ascendancy and strong self-perception of its mission and function legalized through numerous doctrines promoted their position in the Indonesian society once as liberator and now as a center stage actor. It considered itself as a political mediator and unifier of the Indonesian nation. A.H. Nasution the espouser of the military's increased role envisioned the institution as a political referee which could step in to and settle disputes amongst political parties but one which would stay above the fray of party politics.⁷² Yet, they have been responsible for Golkar's political preponderance in the last 30 years.

Through numerous Golkar affiliated organizations such as the National Committee of Indonesian Youth (KNPI), ABRI extended its reach into civil society.

This implies blurring of the parameters between military and civilian roles in all spheres of society. The TNI's roles were not defined clearly from its inception, though there is indeed failure on the part of the civilian leadership to define the demarcation or clear lines of responsibility. Soekarno succumbed to military pressures and proposals that consequently increased their involvement in the political, social, and economic matters. The New Order government of Soeharto increased the military's role in politics.

Nevertheless, it can also be interpreted that Soekarno meant it to be as a temporary set-up as it is seen as appropriate to the needs of the times then. The absence of an effective leadership and political institutions under Soekarno are factors to consider as well. In some accounts, Soekarno was forced by ABRI to transfer power to Soeharto in 1966.⁷³ Essentially, during Soeharto's reign, they became the doorkeepers of the expansion of political participation and guardian of the existing order, which clearly exemplifies the Indonesian case. Thus in the ensuing years, we witness a repressive establishment, a deeply entrenched military whose presence overwhelmed the people and consequently losing the public's confidence in the institution.

The Changing Political Dynamics: A New Role for the Military?

As early as 1988, some retired military officers expressed that the military have be-

come too deeply involved in the political process. Benny Moerdani had also begun to sympathize with the view that *dwifungsi* had gone too far and it was time to tone down the security approach to governance.⁷⁴ They became vocal proponents of *keterbukaan* (openness) and called for a democratic culture, though parameters of political debate were still under their discretion. The call never prospered until the events in 1998 struck them like a thunder or it was like an institutional shock and suddenly found itself at its political ebb. Moreover, "ABRI faces its greatest challenge ever. Soeharto's fall (resignation) from power has already generated unprecedented debate about ABRI's place and future role in Indonesian politics."⁷⁵ During the course of 15 years, the military was abused by Soeharto to fight for his political and business interests.

For 32 years, two actors -- the Armed Forces and President Soeharto -- dominated the Indonesian political scene. Though, emerged as the only intact institution after 21 May, its sins from the past brought them down the ladder. The political lid finally opened, civil society demanded for a reduction of their political involvement, and from the other end of the political spectrum called for its complete exit from politics. The latter of course, is quite impossible to achieve at the moment, and would certainly pave the way for TNI's political restiveness. At the same time it creates a political vacuum which would likely complicate the process of change.

A complete exit from socio-political affairs will not happen immediately. This will depend on the extent to which civilian leadership is able to hold the nation

together and resolved urgent political issues. This will be a long and difficult process, especially to an institution that has been in power for the past three decades. Political observer Soedjati Djiwandono said that their exit would largely depend on civilian capabilities, since the military's involvement was copiously attributed to civilian failure to govern and hold the country together.⁷⁶

This view has posed a big challenge to the civilians themselves, as they have to earn legitimacy and at the same time have strong claims to political authority. With result of the June 1999 elections secured, they were able to pass their first political exam -- a denotation emphasized by General Agus Widjojo -- Commandant of the Command and Staff College (*Sesko-ABRI*) in Bandung.

The Changes and a New Paradigm

In an atmosphere of greater political openness, the military is under pressure to lower its political profile and reform itself. With the ebbing of the President's legitimacy, the institution was placed in a tight spot, where the only maneuver is change. The institution cannot invoke the "savior of the nation" phrase to the people. The liberal environment compels them to change, consequently erode its political stature in society. Moreover, the possibility of its institutional interests, such as keeping Islam at bay, undermined.

According to a military observer, the political involvement of ABRI had been too deep and too long. It has resulted in the breakdown of the mechanism of military personnel achievement that was basic-

ally based on professionalism. At this point, the military seems to suffer low-key cohesiveness and thus, the role of the leader of the establishment is to balance the forces and clear up its image, its lost credibility and pride.⁷⁷ The most immediate step that the military leadership should do is to bring ABRI back to its basic identity, and strengthen ABRI's intelligence unit and capability to mobilize troops to cope with social riots especially in the situation like the June 1999 elections.⁷⁸ These steps, however, would be meaningless unless accompanied by ABRI's efforts to restore its credibility.

First among its agenda is to correct its repressive policies. Habibie himself, as a political posture, expressed his deepest regrets for the human rights violations committed by the military.⁷⁹ The military for its part started to put its house in order by discharging Lt. Gen. Prabowo, for the abduction of 2 dozen dissidents in early 1998.⁸⁰ Further, in 6 April 1999, eleven members of the KOPASSUS were sentenced 12 to 22 months for kidnapping nine political activist months before Soeharto resigned. The court decision, for the military is seen as its fulfillment of its obligation to complete the investigation,⁸¹ for the public, the big fish is still out in the ocean.

Nevertheless, from an interview with political observer Kusnanto Anggoro, the military talks about redefining their doctrine but they are actually unable to do very important things, like resolving the Trisakti killing, and the involvement or non-involvement of Gen. Prabowo of KOPASSUS. Discharging a military official and expression of apology are inadequate to compensate for decades of political

repression people underwent. The image building will take a long time to construct and winning public trust will involve confidence building over an extended period.

It must be noted that the Indonesian military did not openly oppose *reformasi*, they have also undertaken some changes that connote their support to the reform movement. Even before Soeharto's resignation, new generation of ABRI generals now taking charge of key military positions is in favor of changing the old ways.⁸² Planned changes within the military are laid out in a document entitled "ABRI in the twenty-first Century: Redefining, Repositioning and Reactualizing of the ABRI's Role in the National Life."⁸³ Gen. Bambang Yudhoyono, one of the few military officers who see that the military should not be too involved in politics, pointed out "that the Armed Forces is now repositioning itself and redefining its dual function in defense and politics."⁸⁴ He added that they are focusing on their main role in defense and security and will gradually reduce role in society.

The Armed Forces acknowledged its faults in the past and are readjusting to the changing times. Soeharto's distortion of the role of the Army and the implementation of its doctrines were the fatal mistakes committed by ABRI.⁸⁵ One officer said that their loyalty belongs to the United Nation of Indonesia now so as to avoid distortions. Roughly translated⁸⁶ by an ABRI officer, part of the new paradigm of the Armed Forces is as follows:

- (1) Separation of the police and ABRI;
- (2) Liquidation of political affairs in the local level;

- (3) Changes in socio-political affairs to becoming the territorial staff;
- (4) Liquidation of civilian positions from central to local governments;
- (5) Liquidation of civilian socio-political affairs in the military regional command until the lowest level;
- (6) Choose between civil and military positions either they retire or be in the military;
- (7) Reduction of the number of ABRI in the parliament in the local and central;
- (8) ABRI promised not to be involved in day to day politics;
- (9) Cut organizational linkage with Golkar and have distance and exercise neutrality towards political parties;
- (10) Commitment and consistent neutrality of the Armed Forces in Elections;
- (11) Change the new paradigm of the relationship between ABRI and ABRI's big family relationship;
- (12) Revision of the doctrine according to the spirit of reformation in the 21st century.

The above paradigm is yet to take a concrete form and shape, though some have been in effect for months such as choosing between staying on in a civilian office or going back to active service. Effective 1 April 1999, the police had been separated from the ABRI. Yet its internal security function is not exclusive to the police establishment. With the enormous internal security-related problems, the police will call on the military for support or if not, place hot spots under the military command. Furthermore, the police will still

report to the defense minister, who happens to be Commander of the Armed Forces as well, and not to civilian local authorities.

Hence, the separation is still unclear whether maintenance of law and order will be solely under the military's command or whether the separation is just ceremonial. In effect, it will not affect its previous internal security function but may "form part of the beginning of the right process towards independence of the police force in the sense of putting it in its proper place as guardian of public order and security, as law enforcement agency."⁸⁷ It would at least be a step towards clearing up overlapping functions with those responsible for the external defense of the country. In this respect, the development in the international and regional strategic environment will influence the shift of defense priorities of the TNI. In the meantime, restoring law and order and resolving domestic social and political violence in the country are the current priority.

In spite of the reduction of its seats in the House of Representatives, the revocation of *dwifungsi* has been called by the pro-reform group. However, one military official stated that even if the military withdraws from the socio-political sphere, it does not mean that they will withdraw their concern for the country.⁸⁸ How this expression will take shape is yet to be determined. This statement is still reminiscent of the years when the army thought that they must take an active part in all aspects of society.

On ABRI's big family this means that members of the family do not have to toe the party line since their institutional link

with Golkar has been terminated. They may vote who ever they want. The single majority is outdated, thus the political choice has widened from three parties to forty-eight (48).

The above changes would take some time to implement, but observers say that the military is not clearly stating its withdrawal from socio-political affairs. It is too early to say whether the above will transform the military but definitely there will be changes. Most scholars would conclude that the Indonesian military has always been an exception to the general rule on political developments. Noticeably, ABRI keep on reminding the public that they will not intervene in the political process.

Failure to Thread the Nation

On hindsight, the military is ill prepared for the social and political outbreaks in Indonesia. J. Kristiadi revealed that this is partly because of poor intelligence operations of the army, which must be addressed to curb the social unrest and build an early warning system. Another is that the phenomenon is something new since they only know the following threats: the extreme left (communists), extreme right (Islamic fundamentalism), and those against Soeharto and Pancasila. What's happening now for them is new *Suku, Ras, Agama, Antar Golongan* (SARA)⁸⁹ things that have been swept under the rug for decades.⁹⁰ Moreover, they have been trained to use heavy-handed measures, which is now being heavily criticized and extremely abhorred by the people. The army even revealed feelings of uncertainty on how to deal with the violence. The prevalence of the breakdown of law and order in the

country indicates their inability to curb the outbreaks.

Their inability and failure to keep law and order in several cities hit by riots and upheaval have been on going before and after the Soeharto's fall.⁹¹ The army no longer enjoys the stature as savior of the nation and has in fact, according to Soedjati Djiwandono, dismally failed to ensure the security of the people, which is its first and primary function. Riots and killings in Java and in Central Jakarta exemplifies this point. The civil unrest from all fronts is straining the armed forces and Major General Agus Wirahadikusumah admitted, "it is not completely in the hands of the military."⁹²

The military failed to avert the slaughter of Madurese by the Dayaks, it also failed to thwart the escalation of the violence in areas considered as flash point. The handling of violent outbreaks in East Timor between the pro-integration and the pro-independence groups is another example. There are suspicions that the military is arming the pro-integration group, which an independent move from some sections of the establishment. "It is also possible that some elements of the army leadership do not like Habibie's new approach to East Timor and are trying to subvert it on the ground."⁹³

A military officer asked about the division on the East Timor issue, denied the cleavage, although did not discount the possibility of the existence of emotional sentiments. It is understandable, according to Gen. Agus Widjojo, since anybody has feelings and its human nature, but has not transformed into a real physical movement. Moreover, there are neither traces

nor support for it. Some quarters believed that the continued inability is a way to justify its role as the purveyor of stability.⁹⁴

The military has so far announced that they would enhance co-operation with all elements in society to help defuse the crisis and to maintain national unity. Who would say that the bedrock of the country's stability is also, failing, it is a new historical experience for the military, where their presence is abhorred and where victory over threats of disintegration has been very elusive in the last two years.

For the military, threats would emanate largely from internal sources. These include the results of national development and the economy. Civil society in general should not be drawn into euphoria, according to a military officer.⁹⁵ Further, the military can clearly understand, but as a nation, they should consolidate and establish a system to sort out those procedures, taking advantage of the positive effects and neutralizing negative effects. In neutralizing negative effects, no tinge of repressive attitudes, though the military will have to maintain law and order and open channels of political communication.

Mutual Suspicion

One can draw a conclusion that the dominant position of ABRI will gradually reduce or even disappear, when the situation become "normal", when civilian political forces are politically able to govern. In addition, when civilians according to the military were able to free themselves from "saboteurs." In other words, the *dwi-fungsi* of ABRI will always try to strike some dynamic balance between the civil-

ians and ABRI.⁹⁶ At the moment, the balance is nowhere in sight and who determines whether the civilian political forces are free from saboteurs?

Doubts have been expressed by the military about civilian capabilities to govern.—The country is too fragile thus needs someone capable to lead and manage the country as well as have the required national outlook. Albeit the meaning of what kind of national outlook is required remain unclear. Rizal Sukma in an interview however, said that some concerns of the military is legitimate like who is going to decide what they need in terms of budget, arms procurements, defense interests and so on. Analysts are in agreement that as of moment, no civilian has the capability to take-over defense matters or become Minister of Defense. Though public pronouncement indicate that they will support who ever will be the next leader of Indonesia, civilian or otherwise. The military is also apprehensive about civilian intervening too deeply into military affairs just like in 1955, that will consequently “spoil” the management of the Armed Forces.

Yet the expression of doubt is a mutual political feeling that may be exacerbated by General Wiranto's acceptance of his nomination as Vice President for Golkar. His nomination is ill timed when civilians are enormously wary of the military's intentions and role in maintaining the status quo and at a time when the nation is entering an era where the axis of powers has changed.

Retired officers doubt the neutrality stance of the military. Major General Su-

warno Adiwidjojo said that it is still rhetoric and the public still waits for concrete action and guarantee from the Armed Forces of its neutrality⁹⁷ even after the elections. The military will likely mobilize its resources to insure Wiranto's election. Though, he rejected initial nomination as candidate of Golkar as President. However, sources say that Wiranto will reject the VP nomination because it will affect their neutrality stance at this crucial period in Indonesia's history.⁹⁸ However, some believed that he might change his mind after the election.⁹⁹ To promote greater transparency in the military appointment to the Parliament, General Wiranto was publicly encouraged by the Election Commission to announce the names of the military officers to be appointed legislators to enable members of the public to air their objection.¹⁰⁰

Even it's so-called house cleaning in 1998, is not sufficient to erode the public's distrust over the institution. “Atrocities committed by the army in Aceh, Irian Jaya and East Timor have fuelled demands for independence in all three provinces.”¹⁰¹ Thus regaining lost respect and trust will take time and meanwhile clouds of doubts hovers civil military relations in Indonesia.

Now and the Future

*Now that we are inheriting the republic, we don't want to be responsible for its falling apart.*¹⁰²

Major General Bambang Yudhoyono, Deputy Chief of Staff for Socio-political Affairs.

The above expresses the sentiment of the Armed Forces, yet there is certainly a gap between the civilians and military

in terms of power sharing. The decision to gradually withdraw the process will be as slow as redefining their role that need to be spelled out. Historical circumstances defined their role in society but narrowing the gap will take some time to equalize. Whereas civilian distrust in the establishment will surely serve as a checkmark of the political imbalance. A scholar commenting on the process said that how fast this equalizing process will materialize depend on the course of Indonesia's political development since the situation is still very volatile. It will also hinge on how regional political developments would impact on the defense priorities of the Armed Forces such as China's security and military posture in the region.¹⁰³

It has to be understood that the military see their connection with the whole national system. They are not independent from it and thus do not exist in isolation. Hence, Claude Welch's statement that the military cannot be prevented from participating in the political process is a reality in Indonesia. ABRI acknowledged that during the New Order, it has enjoyed the umbrella provided for its socio-political role. However, the political format now is different and the military is at the bottom pit in terms of reputation and image. It mishandled many of its operations and concrete manifestation of which is the military's failure in Aceh and in East Timor.

Official pronouncements from the military is that ABRI's role both now and in the future, can be analyzed from a number of different perspectives: historical, dual function and socio-political affairs, and social perspective. In the spirit of democratization, ABRI has undertaken not only to

fully support the reform movement, but also to take part, and become an integral component of it. These are vague pronouncements as to how they will take part, however, how they will become an integral part of the polity is not yet concrete. It seems that the historical justification will tarry for now, but the people will have to actively guard their excesses. However, to enable civil society to make a political vigil, political rights must be guaranteed.

"TNI's withdrawal from politics is an absolute requirement for democracy, only if the military pulls out politics."¹⁰⁴ In this view, the TNI should not play a leading role in the next presidential elections, according Lt. Gen. Hasnan Habib (ret.). Notwithstanding, General Wiranto has kept his silence over the reported plan of Golkar to nominate him as Vice President. If he changes his mind after the elections, his closeness to Soeharto and career shift as well is too short and will most probably be greeted with doubt, as this would likely mean eating the same old cake, representing still the New Order. He and Habibie are not credible to lead the political and economic reforms since they have been influential and are very much identified with Soeharto.

Most scholars say that the future role of ABRI is still unclear, as political development itself is unpredictable. The political outcome in June gave credence to the military's neutrality stance but ensuing event is still fluid and thus difficult to discern. The military's neutrality certainly played a crucial role at this particular historical conjuncture. Though they can play a very positive role in socio-civic missions

and civilians themselves can assist the military through training on conflict resolution¹⁰⁵ which in the long run will be more acceptable to the civilian polity but how far can the military shed its role in society?

There is no retreat to democracy, the military role will eventually be reduced -- but the extent of its reduction is still underway and how long it will take are still unanswered questions. It has reiterated its commitment to reform, setting the following as agendas:

- (1) new paradigm (the military) doctrine;
- (2) structure and posture (organization);
- (3) education programmes;
- (4) training programme;
- (5) ethics;
- (6) leadership.

The above were designed to improve its tarnished image. This big project that should not be delayed, re-thinking their role in politics and going back to the basics will pre-occupy them in the next millennium. Involvement of civilian in re-defining their doctrine and their mission is eminent. Their sins of the past have greatly damaged their reputation as well self-confidence, making it harder for them to maintain order and prevent outbreaks, thus, the failure to thread the nation.

Nonetheless, the military has no tradition of coup d'état, in part because *dwi-fungsi* is a constitutionally provided privilege giving them an institutionalized role in politics. Reduction of its role as social and political managers must also be institutionalized. It should also be noted that direct military involvement will not likely occur since, according to some observers and military officials said that such

action is not conducive to the environment and will not be acceptable to the polity as Indonesia faces uncertainty.

Timetable of the military's withdrawal is yet to be agreed even the process of withdrawal will have to be worked out. According to Sukma, the military is not comfortable with the timetable initially drawn up by the civilians. Moreover gradual withdrawal has been promised 10 years ago but the civilians do not buy it anymore.

Current civil military relations in Indonesia are a new chapter in their history. One, civil society are more politically assertive and the military still in the midst of re-defining its role. Two, it is characterized by mutual suspicion. The civilians questioning the military's sincerity to carry out reforms and rejecting its role. People still feel that the military's excessive role in politics caused a lot of political damaged. The military on the other hand is doubtful of civilian capabilities, which are historically rooted. Even the civilians admit that at the moment, there is no competent civilian that can take over defense matters.

When and how the military will go back to the barracks are questions asked by the civil polity. Though there are indications that they will withdraw and signs of support for the current transition process. Definitely there will be no popular support should the military intervene directly in politics. It would take some time and would depend on whether the new government can cope with the situation.

Robin Hays wrote how the military and security institutions can contribute to democratization.¹⁰⁶ One of them is civic military

action in disaster coordination, humanitarian assistance and nation building projects such as public works. Moreover, the institution can also serve as peacekeepers during elections. A Thai retired military general¹⁰⁷ said that the role of the military in the transition process is to keep out of politics and play a positive role by ensuring a fair and free elections. At the same time, it should also create a climate that would ensure the above.

The military's gradual withdrawal must also be accompanied by re-orienting its defense and strategic doctrines by focusing more on defense of sovereignty and external security functions. Another is to depoliticized military through indoctrination and training emphasizing military's role in external security of the country. Bridging the huge gap between the civilian and military in Indonesia will take time and these are some future thoughts for the military and the civilians as well.

Concluding Notes: Crossing the Road

Crossing the road of the transition process is not a tractable endeavor while facing economic, social and political crises. Indeed, Soeharto left Indonesia with a weak government and the army, an eroded public image, who has to cope with persistent communal and racial violence, separatist movements and social cleavages, exacerbated by the worst economic recession in 30 years. One important task is how to organize its society addressing regional economic and political imbalances, and discourse on decentralization and autonomy will likewise take center stage in the years to come.

The general election in June 1999 certainly provided fresh mandate and ex-

pectedly a fresh start for Indonesia. It is the first democratic political experience of the country and the June electoral exercise seems to be the anchor that would tow the nation to the road of reforms and transformation. The commitment to reforms and demokrasi must be sustained by the new leadership is likewise critical. The problem of the pro-reform is how to make all political forces work together and solve the social and economic cleavages that threatens to undermine political order.

Another task is amending the constitution. The Constitution that was drawn in 1945 is a very tentative one and drafted posthaste without setting a clear limit on the term of office of the President. At the same time, this should include articles that will guarantee political rights and avenues that will enable the larger society to participate and express grievances.

The rise of Islamic political parties, which should have occupied an ample space in the paper, was initially opposed by the military.¹⁰⁸ The Islamic-based parties have been politically marginalized for more than three decades because of the military's historical apprehension on Islam militancy and perception that they are a threat to the unity of the country as well as to the *Pancasila* doctrine. At the same time, there exist separatist movements identified with Islam in North Sumatra. However, because of years of political isolation, Islam political groups are split and thus, the threat is more of using religion to incite unrest and conflicts. The bombing of the offices at Istiqlal is one attempt to stimulate religious violence. Their proliferation is an inevitable consequence of the opening of the political doors after Soeharto's resignation.

Depending on what the Indonesian civilian polity may agree on, ideally, the holders of the instruments of coercion should not actively take part in the political sphere. The military unable claim credit for the current transition process -- the blurring of the role -- is still present evident in the retention of their seats in the MPR, though the number of seats reduced. They see their interdependence with the whole system and hence, will have to stay for a while. The role of the military is still unclear as the institution itself undergoes a process of transformation while the whole nation undergoes the same process. It will be a political shock for them to completely exit from the socio-political spheres after decades of political preponderance. It will also create a political vacuum should they withdraw altogether since many of them are either governors or serving as regents. In this case, a well-defined role for the military in the post-election period must be drawn-up. Thus:

- Civilians and the military should develop new definition of the military's role as well as determine the political boundaries.
- The police should be separated from the military, if truly TNI wants to "civilize" the institution.
- The civilian polity has to be strengthened by providing adequate political space and freedom to air political grievances. At the same time, increase their capability to govern without relying too much on the military.
- The gap between the military and the civilians must be addressed and at the same time the military has to re-orient its mission and doctrines emphasizing on the value of professionalism.

- Addressing human rights issues by the civilian and military leadership.

Though they talk about reforms, there is no clear statement of their withdrawal. However, one military general stated that the role that could be played by ABRI is what ABRI has played in the Habibie transition and that is shaping the environment without direct involvement. But clearly, the military is no longer the unifier and savior of the nation. They are beat up and over stretched, as people no longer revere them as they used to. Even the "troops freely admit to feeling the strain of constant confrontations with hostile crowds." Though, in the long run the military can play active role in socio-civic missions such as disaster management, engineering activities in the countryside and as peacekeepers in areas where potential communal and ethnic violence are very high. Prior to enacting a role in transition, the trust and confidence of the civilians and the military must be built first. Confidence building programmes must be instituted to accomplish this task, a crucial step towards transition and eventually consolidation.

Will there be civilian supremacy in the long run? It is too difficult to determine, it is a western political concept that is hard to sell to the Indonesian military. Civil-military partnership is more palatable. The problem is how to define division of labor between what is military and what is civilian. Where do military operations end and when does civilian authority begin? The civilians will have to assert themselves and can only be done by earning the legitimacy currency and putting the house in order.

As a new democracy, "reducing the power and privileges of the military establishment to a level compatible with the functioning of a constituted democracy will be a problem to the new leaders." Yet the harrowing internal unrest must be addressed thus the institution will continue to dominate domestic security operations.

As the country attempts to put its house in order, political uncertainty pervades. Soeharto's resignation on May 21, 1998 did not certainly bring forth-substantial changes, yet opened the political doors. The military during this period is still searching for its role in society while the country faces cleavages brought about by the June 1999 elections. As political and economic expectations rise thereafter, the military has to come up with concrete measures and reforms for retrieving society's confidence. In turn, civilians should not create a pretext for military's increased role in politics that could be manifested through total break down of law and order that may threaten the unity of the nation. Democratization in Indonesia will continue to be challenged by divisive issues that impact on the current political and economic landscape. Finally, economics must be simultaneously addressed while the house is being swept clear of political baggage. Further, the military will have to be a partner in crossing the road towards democracy.

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ASEAN and the ASEAN Regional Forum: Should "The Driver" Be Replaced?*

Rizal Sukma

Introduction

WHEN the first meeting of the ASEAN Regional Forum (ARF) was convened in Bangkok in July 1994, foreign ministers of eighteen Asia Pacific's players agreed to give the new regional undertaking a modest start. It was agreed from the outset that such unprecedented experiment in multilateral security dialogue within the Asia Pacific context should not be impaired by the desire to pursue an ambitious plan through a rigid institution. To that effect, the main objective of such undertaking was then expressed in general terms. Rather than setting out a set of concrete objectives, ARF foreign ministers recognized "the need to develop a more predictable and constructive pattern of relationships for the Asia Pacific region." In that context, it was agreed that the ARF provided the opportunity for Asia Pacific countries "to foster the habit of constructive dialogue and consultation on political and security issues of common interest and concern."¹

With such an initial blueprint, the ARF has attracted wide interest from within and outside the region. It managed to begin the process with 18 founding members in 1994, including the United States, China and European Union (EU). As the process progressed, the United Kingdom and France have occasionally expressed their interests in becoming full members separate from that of the EU. In July 1998, Mongolia became its twenty-second member. However, five years after it was formed, the ARF continues to attract intense debate between supporters and detractors alike. Much discussion on the value of the Forum generally revolves around the nature of the grouping as an ASEAN-led process, the nature of progresses it has made and, more recently, the merit of ASEAN's role and the relevance of "ASEAN Model." The debate has been so well documented to the extent that any attempt to put the ARF into investigation will face the risk of becoming redundant.

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This paper, however, is not meant to provide a radically different interpretation and analysis of the ARF. It seeks to

address the usual and familiar themes but in a somewhat different context. While earlier discussion on the ARF has been marked by a clear division line between defenders of conservatism and advocates for change, the present paper seeks to address the strategic need for ASEAN to preserve the value of conservatism on the one hand and embrace the imperative for change on the other. For the purpose of this paper, the arbitrary emphasis on ASEAN -- as opposed to the ARF as an institution -- is indeed justified not only because of the Association's institutional and administrative centrality within the ARF, but also due to the fact that the success and failure of the ARF have often been associated with the strengths and weaknesses of ASEAN in administering and driving this experimental regional undertaking.

In so doing, the discussion is divided into four sections. The first section discusses the nature of ASEAN's leadership role in the ARF. The second section examines how the ARF has functioned to date and discusses the underlying reasons behind ASEAN's continued claim to be in the driving seat. The third section discusses the challenges facing ASEAN in driving the ARF process, especially in terms of the impact of the crisis on ASEAN's credibility, challenges from major powers, and the limits of the "ASEAN Way." The final section addresses some adjustments that ASEAN needs to take in order to preserve the Association's institutional entitlement to be in the driving seat on the one hand and improve the Forum's relevance and utility on the other.

ASEAN "Leadership" in The ARF: The Case for Strategic Convenience

The fact that ASEAN has been in a position to undertake "the obligation to be the primary driving force" in the ARF process often serves as the main focus of criticisms. The relevance of the ARF as an instrument to cope with post-Cold War regional security problems, for example, has been linked to the organizational centrality of ASEAN in the ARF. On this point, Michael Leifer maintained that "the issue of relevance is reinforced by ASEAN's insistence on retaining the central diplomatic role in the ARF which confuses power and responsibility and generates frustration among North-east Asian and Pacific participants."² In a more direct manner, Robyn Lim declared that "the ARF can do little to promote security because ASEAN insists on its primacy in it."³ More recently, Henderson is convinced that "if ASEAN continues to chair the ARF, the dialogue could stagnate."⁴ In short, all these views maintain that ASEAN's position and role as "the primary driving force" pose a major problem for the ARF process.

ASEAN is also criticized for its conviction and determination in transposing the ASEAN's experience in managing regional security within a wider regional context. In this case, the ARF is often seen to have suffered the same defect that ASEAN has not been able to overcome. For example, it has been declared openly that "ASEAN is an inappropriate model for the ARF" because "the political, economic, and strategic considerations that have made ASEAN a success within South-

east Asia do not necessarily apply to the more powerful states of the Asia Pacific region.”⁵ It has also been argued that “to the extent that the ARF has been created in ASEAN’s image, little more may be expected of it.”⁶ All in all, the “ASEAN model,” which initially served as a prerequisite for the establishment of the ARF, is now considered as an impediment to the ARF process itself.

Such criticisms on the centrality of ASEAN’s role and model in the ARF process clearly raise a broader and more fundamental question: to what degree is ASEAN leadership still vital, necessary and adequate? Before we can answer this question, it is important to pose another question: why and how has ASEAN come to play such a leadership role, and under what circumstance? Standard argument advanced by “ASEAN apologists” -- that ASEAN is entitled to play such a role because the ARF was an ASEAN’s creation -- does not help much to convince detractors and critics alike. It can be argued instead that ASEAN did not ask to play such a central role, but that role went to ASEAN primarily due to unique historical and strategic context at the time of the founding of the ARF itself.

Four reasons can be presented to support the above argument. *First*, ASEAN leadership role was indeed vital in the founding of ARF. With the end of the Cold War, there were growing calls in the region for the creation of a multilateral security forum in which states can address regional security issues. However, such calls were received with suspicion

and rejections by both major and lesser powers. Initial proposal by Australia and Canada in July 1990 that such forum be modelled on the Conference for Security and Co-operation in Europe (CSCE) was rejected by the US due to Washington’s deep suspicion of “any prospective multilateralism in the Asia Pacific that might undermine the utility and credibility of existing bilateral arrangement to which the United States was committed.”⁷ The proposal was also resented by ASEAN states as “‘inappropriate’ security concept being foisted on them by outsiders,”⁸ arguing that “what worked in Europe could not be transplanted to Asia.”⁹ China, on its part, has always been wary of multilateral approach to security, especially if the proposal was made by major powers.

When ASEAN then recognized that the drive towards multilateral security structure was hard to resist without risking itself being marginalized, it quickly developed the idea of using the ASEAN-PMC to serve as a model for the needed multilateral security forum. The reality of post-Cold War marked by precarious pattern of relationship among major powers, especially among the US, China, and Japan, served as an important factor that presented a rare opportunity for ASEAN to advocate its own model of multilateralism based on ASEAN’s experience in regional undertaking, albeit in a much different context. As the initiative came from a grouping of lesser regional power, the major powers were presented with an idea of which they had no significant reasons to oppose. Indeed, ASEAN’s proposal was accepted because

"the Association was an acceptable interlocutor to all the major powers."¹⁰ During the ASEAN-PMC meeting in Singapore in July 1993, it was then agreed that a multilateral security forum, which was later known as the ARF, should be created. To that effect, ASEAN's role in bringing the ARF into existence could be regarded as vital indeed.

Second, as a logical consequence of the first reason, ASEAN's leadership role was indeed necessary to ensure that what had been agreed in Singapore in July 1993 would not stagnate soon after it was initiated. As the formation of the ARF was made possible by ASEAN's vital role as an acceptable interlocutor, then an immediate attempt to marginalize ASEAN's leadership role would obviously undermine the very reason why the ARF was accepted in the first place. In this context, it has been noted that beneath the consensus among the major powers on the creation of ARF "lay support for ASEAN's leading role in promoting the multilateral enterprise."¹¹ A continued ASEAN leadership role in the ARF therefore served as a necessary insurance for reluctant major powers that the newly-established forum would not turn into an arena where either of them would attempt to pursue a dominant leadership unacceptable to others. In other words, ASEAN leadership role in the ARF after its establishment was necessary to keep the process going according to the way it was expected to be.

Third, given the above constraints, it can be argued that ASEAN had played an adequate leadership role, in which it

only played an administrative role in the ARF process. Such a role had to be undertaken by ASEAN out of necessity, not so much as the result of a well-calculated strategy. Even though the US and China, two major powers that were initially reluctant to embrace multilateral approach to regional security, finally gave their measured support, they extended that support for different reasons and with different expectations. Western states (particularly the US and Australia) expected the ARF to address issues of contention in the region and moves along faster track. At the other end, China was reluctant to move hastily not only because of fears that Western countries dominate and dictate the process, but also due to the fact that its involvement in a multilateral regional security forum such as the ARF was a new undertaking. Therefore, "the ASEAN countries are conscious of walking a line between keeping the impatient West interested in ARF and not moving too quickly for the suspicious Chinese."¹² It was out of this consideration, or necessity for that matter, that ASEAN endorsed the formula that "the ARF process shall move at a pace comfortable to all participants."¹³ In ensuring that balance, ASEAN "leadership" role as an administrator for ARF, seemed adequate.

Four, the absence of open opposition to ASEAN's administrative role, expressed rather hyperbolically in the acceptance of ASEAN as the party that "undertakes the obligation to be the primary driving force," also owed to the fact that ASEAN at the time was widely acknowledged as a regional organization with a

degree of success not only in building institutional identity and in managing Southeast Asian regional order, but also in showing its diplomatic ability to act as a unitary entity towards the outside world. Its past achievements, albeit a mixed one, in bringing order and stability to Southeast Asia commanded some respects within the wider international community. Hence, ASEAN was then often depicted as a success story of a regional grouping -- a compliment that is rarely given to other regional organizations.¹⁴ Indeed, while the ARF may not have yet turned into a perfect security organization, ASEAN's administrative role in driving the process did contribute to the progresses it has made over the last five years.

It is important to note, however, that one should not overstate the nature of ASEAN's leadership role in the ARF. The four reasons discussed above also point to a not-very pleasant interpretation: that ASEAN's "leadership" role in the ARF is the result not only of an act of corporate political will, but also of the strategic convenience. ASEAN's centrality in the ARF process is acquired not by design in the sense that the position was secured as a result of ASEAN's skilful diplomatic exercise, but more by default in that such central position was *given* and *entrusted* to ASEAN primarily for the reason of strategic convenience. In fact, despite all sort of problems it is still grappling with, "ASEAN's model" also serves as part of the solution in the absence of alternative mechanism to deal with the new regional security environment of post-Cold War Asia Pacific.

The opportunity to undertake such a unique leadership role was also presented to ASEAN by objective strategic reality in the pattern and practice of major power relations in the region after the Cold War. In this context, Leifer aptly described ASEAN central role in the ARF as the result of "the fact that the major Asia Pacific powers have been incapable of forming a concert arrangement among themselves."¹⁵ And, ASEAN's past experience and mixed achievements in managing regional security within Southeast Asian sub-region lent additional credibility to the Association's appeal to be in the driving seat. In the absence of similar undertaking and experience in a wider Asia Pacific region, the ARF -- in which no major powers assume dominant -- appeared as an experiment worth trying. For major powers, ASEAN's approach that emphasized confidence-building measures in the ASEAN's approach, undertaken primarily through dialogues, would not do any harm to their national security and strategic interests. It was within this unique context that the acceptance of ASEAN's role as "the primary driving force in the ARF process" should be understood.

After Five Years: The Case for Continued ASEAN's Central Role

It has been five years since the inception of the ARF in July 1994. Yet, as mentioned earlier, the criticisms are still growing and even take a new dimension and pose a more fundamental challenge. The centrality of ASEAN's role within the ARF process has now become the main

locus of reservation, objection, and criticisms. If one argues that "if ASEAN continues to chair the ARF, the dialogue could stagnate,"¹⁶ then one is forced to believe that the ARF will flourish and progress if it is not chaired by ASEAN. In this regard, there are two related questions that need to be addressed. *First*, has ARF functioned so bad under ASEAN's leadership that the Forum needs a fundamental structural change? *Second*, if ASEAN relinquishes its leadership position, will ARF function better?

Recognizing the Progress: Slow, But It Moves

It should be made clear from the outset that the ARF should not be asked to carry out the functions it does not intend to serve. Nor should it be forced to serve all the functions at one time. ARF is meant to provide a formal venue for regional countries to address and discuss regional security issues. It reflected the growing recognition by regional countries on the need to manage post-Cold War security environment through a region-wide multilateral security institution. When the first ARF meeting was convened in Bangkok in July 1994, it was recognized that "the ARF had enabled the countries in the Asia Pacific region to foster the habit of constructive dialogue and consultation on political and security issues of common interest and concern."¹⁷ It was at this first working session that the ARF was tasked "to make positive contributions to efforts towards confidence-building measures and preventive diplomacy in the Asia Pacific region."¹⁸

At the second ARF Meeting held in Brunei in August 1995, it was agreed that collective approach to security would take place "in three broad stages, namely the promotion of confidence building, development of preventive diplomacy and elaboration of approaches to conflict."¹⁹ It was also at this meeting that the importance of transparency, as a means to reduce misperception, was translated into specific measures calling for member states i.e.: (1) to submit to the ARF or ARF-SOM, on a voluntary basis, an annual statement of their defence policy; (2) to increase high level contacts and exchanges between military academics, staff colleges and training; and (3) to soon participate in the UN Conventional Arms Register. The meeting also acknowledged "the importance of non-proliferation of nuclear weapons in promoting regional peace and stability" and noted "with satisfaction the progress made towards Southeast Asia Nuclear Weapon Free Zone."²⁰

At the third meeting held in Jakarta in July 1996, while the Chairman's Statement reconfirmed the ARF's concern over nuclear testing and welcomed the signing of the SEANWFZ, it also supported the ban on the production, export and operational use of anti-personnel mines.²¹ The third meeting also outlined further concrete activities that might contribute to the promotion of CBMs and transparency measures, including:

- the need for continued dialogue on security perceptions;
- the publication of defence policy papers;
- enhancing high-level defence contacts and exchanges;

- circulation on a voluntary basis the same data on conventional arms to the ARF countries at the time of its submission to the UN Register of Conventional Arms (UNRCA);
- the encouragement to work together within the UN to promote more global participation in the UNRCA, and
- call for ARF members to support actively internationally-recognized global arms control and disarmament legal agreements, specifically NPT, Chemical Weapons Convention (CWC), Biological Weapons Convention (BWC), Convention on Certain Conventional Weapons (CCW), and the successful conclusion of CTBT.

By the fourth meeting held in Subang Jaya, Malaysia in July 1997, the Chairman's Statement already noted that significant progress was being made by the ARF. For example, participants of the fourth meeting noted that the ARF "has developed into an important forum for multilateral security dialogue and co-operation in the region." It was also acknowledged that the ARF "has played a positive role in enhancing mutual understanding and trust, promoting greater transparency as well as strengthening the commitment among participants to maintain peace and stability in the region." More specifically, ARF participants noted that "a number of confidence-building measures or agreements made over the years have exerted positive influence on the regional security situation." All in all, the meeting "stressed the importance of consultation and dialogue in enhancing understanding and trust among the ARF participants and in maintaining regional stability."²²

The fifth ARF meeting in Manila on 27 July 1998, while it continued to express the value of "the ARF as an important forum for dialogue on political and security concerns in the region," once again reaffirmed "the significant contribution of the ARF to the establishment of a strong foundation of trust and confidence among its participants, which would be essential in confronting the existing uncertainties in the Asia Pacific region." More importantly, "the ministers noted the growing involvement and participation of defense and military officials in the work and activities of the ARF." Acknowledging that many progresses, especially in the CBMs, have been achieved, the fifth ARF Meeting concluded that "the ARF had been living up to its potential and to the important role it had been envisioned to play in further strengthening the foundations for regional peace and stability."²³

Since official statements are often marked by a degree of diplomatic rhetoric, from the academic point of view it is perfectly legitimate to ask whether such assessment on the ARF's progress really corresponds with the reality. Some scholars have acknowledged that despite its shortcomings, ARF's CBMs activities "are useful in generating a degree of trust among countries which have a history of mutual suspicion" and "ARF workshops have generated a cornucopia of transparency possibilities."²⁴ Such assessment is clearly justified, for example, in the context of growing participation of ARF members in the UNRCA. When it was agreed in the first ARF meeting in 1994 that member states should "promote the eventual participation of all ARF countries in the UN Conventional

Arms Register,”²⁵ participation in the UNRCA had been sketchy. On the first submission in 1993, only three ASEAN members (Malaysia, the Philippines, and Singapore) took part along with China, Japan, US, Australia, Canada, and South Korea. When the ARF convened its second meeting in 1995, 16 of the 19 participants were taking part in the UNRCA (except Brunei, Cambodia, and Laos).²⁶

On the surface, this progress seems trivial because it is not immediately clear how such information could contribute to regional confidence-building process. However, increased participation of ARF members in the UNRCA indicates the growing acceptance of the principle of sharing information on conventional arms in the region. This development also suggests the growing acceptance of the principle of transparency as one important factor in building trust among nations.²⁷ This significant achievement is indeed in line with the primary objective of ARF “to develop a predictable and constructive pattern of relationship in the Asia Pacific”²⁸ by acting as a regional mechanism to mitigate uncertainty and promote transparency. In other words, it is not an exaggeration to say that “there is a growing recognition in the region that transparency in military matters can also enhance regional security.”²⁹

The fact that extensive dialogues and workshops have taken place at an unprecedented rate should also indicate the growing comfort of regional countries with the existing ARF mechanism and approach. Such undertaking, if sustained, would contribute to the rise of the habit of dialogue. As demonstrated in the 30 years

of ASEAN’s experience, the presence of the habit of dialogue and culture of consultation contributed significantly to the institutionalization of self-restraint attitude and mutual respect among member states. Progress achieved in the CBMs area has also been encouraging.³⁰ It has been noted that trust and transparency might reduce the importance of arms which, in turn, could mitigate -- if not eliminate -- the intention to use force as a means of conflict resolution. Indeed, ASEAN governments hopes that the ARF would also emulate the same process with a far more fruitful and productive result.

In sum, it should be acknowledged that despite some initial doubts, the ARF has so far functioned as a vehicle that: (a) introduces the multilateralization of security within the framework of common and cooperative security -- an attempt to seek security with other states rather than against them -- in which major and lesser powers come together and discuss security issues of common concern and interest; (b) lays the foundation and roadmap for a gradual but steady progress in the undertaking; (c) familiarizes the habit of dialogue and consultation as a distinct approach to security as opposed to balance of power practice; and (d) contributes to the process of identity-building among its diverse members. These four achievements, albeit they are still on-going process, indicate a degree of success of the extension of ASEAN approach to security into the wider Asia Pacific region.

Even if one disagrees with the above assessment, the bottom line is that it is important to recognize a major accomplish-

ment of the ASEAN-led process in injecting the habit of dialogue into the wider Asia Pacific region. It has been able to emphasize the merits of multilateralism without discarding the primacy of bilateral approach that still serves as the tenet of American engagement in the Asia Pacific and the core element of China's international relations. Therefore, it is unfair to dismiss that the "comfortable to all" approach has no value for the ARF process. At least, "its very survival is an indication of its important to its members."³¹ Beyond that, the approach has also provided some grounds upon which future progress can and should be made.

Nonetheless, if one expects that the ARF would soon evolve into an institution capable of resolving conflicts, that expectation is certainly misplaced. Regional countries are still dictated by unique security challenges of their own. Similarly, one should not expect either that the ARF will transform itself into a OSCE-type of security organization. Moreover, there is no convincing reason yet why it should move towards that direction at this point of time. The pace of progress in ARF's venture, in which many of its members are still learning about the merits of multilateralism, should also take into account a number of factors such as specific needs and interests of regional states, developments in major power relations, national sensitivity, and the degree of perceived threat.

The above argument is not meant to argue that ASEAN has played its leadership role in a perfect manner. Indeed, there are some truth in some of the criticisms.

Clearly, ASEAN's approach to regional security may have some defects that can be extended to the ARF as well. There have been a number of cases where the limits of "ASEAN model," as applied to the wider Asia Pacific region, can be found within the ARF. The cases of South China Sea, Korean Peninsula and Taiwan, for example, are illustrative in this regard.³² The fact that ASEAN has been criticized for not paying sufficient attention to security issues in Northeast Asia, and the Association's inability to influence some course of events in that region, are well taken. However, ASEAN seems to see that those criticisms only point to the limitations of the ARF, not its failure. On balance, ASEAN is still convinced that given such achievements, there are still not enough reasons for the Association to relinquish its current central role in driving the ARF process.

Indeed, ASEAN continues to insist that it should secure its current central position within the ARF. The Hanoi Plan of Action (HPA) adopted by ASEAN head of states and governments in Vietnam on 15 December 1998, for example, stipulates that "ASEAN's chairmanship in the ASEAN Regional Forum (ARF) process" shall be maintained. It also urges member states to "undertake, actively and energetically, measures to strengthen ASEAN's role as the primary driving force in the ARF." Implicit in this stipulation is that such leadership role is imperative for ASEAN to enhance its role as "an effective force for peace, justice and moderation in the Asia Pacific and in the world."³³

Such commitment to retain ARF chairmanship and the determination to strengthen

its role as the primary driving force is seen as a necessary operationalization of the agreement on ASEAN Vision 2020, adopted a year earlier at the ASEAN Informal Summit in Kuala Lumpur in December 1997, that envisions "the ASEAN Regional Forum as an established means for confidence-building and preventive diplomacy and for promoting conflict-resolution."³⁴

Moreover, ARF members themselves have "commended ASEAN for its important contribution to the ARF process and expressed their support to ASEAN's continuing role as the primary driving force of the ARF."³⁵ This clearly suggests that at the official level there have not been positive signs of impeding change. Despite all the criticisms and mixed feelings about ASEAN's central role in the ARF, and the way it has functioned, there is still a consensus that "the evolutionary approach to the development of the ARF process would be maintained." Indeed, such consensus seems to have been taken as an insurance for continued ASEAN's leadership role in the ARF.

Pulling ASEAN Out of the Driving Seat: Will ARF Function Better?

It has been mentioned earlier that critics argue that the ARF will stagnate if it continues to be chaired by ASEAN. Such argument implicitly suggests that the ARF will flourish and function better if it is led by a non-ASEAN member, presumably the US. However, it is not immediately clear how an ARF with a non-ASEAN member in the driving seat can bring about a fundamentally better result than what it has already achieved so far. On the con-

trary, there is a reason to worry that the future of ARF process might become more uncertain. If ASEAN's leadership in the ARF is seen as the cause for stagnation, than the leadership of a non-ASEAN member could lead to its demise. The reason for this lies in the nature of major power relations, especially among the US, China, and Japan.

Criticisms on ASEAN's centrality in the ARF were generally launched within particular context and at a particular point of time. In this regard, improved relationship among the regional major powers often formed the basis for argument on the decreasing value of ASEAN leadership in the ARF. It was argued, for example, that "should the trend toward multipolarity continue, with strategic partnerships among the major regional powers leading to an emphasis ... on great-power consultations and great power-led subregional security dialogues, the ARF is bound to recede further in significance."³⁶ Improved US-China relations after Clinton's visit to Beijing in June 1998 seems to have informed such analysis.

In fact, the existing pattern of relationship among the major powers, marked by a degree of suspicion and competition, has not been radically different from what it was five years ago. Relationships between China and the US on the one hand, and between China and Japan on the other, are still problematic. That is more so since the strengthening of the US-Japan alliance in April 1996 and the worsening of US-China relations due to a number of issues such as the bombing of Chinese Embassy in Beograd and Washington's allegation that

China has stolen sensitive military technology from the US through espionage. Indeed, as one analyst puts it, "the US-China 'strategic partnership' is nonsense."³⁷ Under such fluid condition, any attempt by the US to play a dominant role in the Asia Pacific region, especially in the ARF process, will certainly invite strong resistance from China. For its part, the US will not see any strategic incentive in endorsing a Chinese-dominated ARF process.

For the foreseeable future, therefore, it is still difficult to imagine how the ARF will work if the US or China assume the driving seat. The strategic convenience factor mentioned earlier has not lost its relevance yet. The relevance of Leifer's argument, in which he maintains that ASEAN's central role in the ARF was the result of the inability of the major Asia Pacific powers to form a concert arrangement among themselves, is still evident. Indeed, strained relations between China and the US and between China and Japan continue to reinforce the fact that ASEAN's leadership role in the ARF is only the result of strategic convenience due to the fluidity in the major power relations. The irony, however, is obvious: while recent developments in China-US-Japan relations could be detrimental to regional security and stability, it nonetheless has worked to the advantage of ASEAN's claim to be in the driving seat.

Nevertheless, it would be naïve to argue that ASEAN's determination to keep its central role in the ARF process is not without challenges, especially since the outbreak of the economic crisis in July 1997. Similarly, it would be misleading also

to argue that there is no need for ASEAN to undertake some necessary adjustments. As the crisis is likely to intensify internal and external challenges to ASEAN, there is strong evidence to argue that ASEAN is indeed faced with a difficult task of overcoming the crisis and restoring its credibility as a successful and respected regional player. Only then will ASEAN's entitlement to be in the driving seat be taken seriously.

The Challenges Ahead: Credibility, Major Powers and the ASEAN Way

Crisis and the Question of Credibility

With the outbreak of the worst economic crisis since July 1997, a number of ASEAN countries have suffered serious economic downturn. It served as a strong reminder that the main security threat to the region still stems from the interplay between internal problems and intra-regional sources of conflicts. The crisis, which started with the fall of Thai Baht, clearly demonstrates that what at first seemed to be an internal economic problem of an individual state could in fact have serious consequences to the whole region. When the contagious effect took its next victims in Indonesia, South Korea, and to the lesser extent Malaysia, then the whole East Asian region was in disarray. The story of Asian economic miracle, which was initially portrayed as a skilful display of regional success in tapping the economic benefits of globalization, has now turned into a story of regional despair. More importantly, the economic crisis has aggravated both internal and external chal-

allenges that ASEAN has to face since the end of the Cold War.

For ASEAN, the crisis presented an overwhelming challenge in overcoming the domestic turmoil in several member states and its implications for broader regional security issues. It is unfortunate for ASEAN that the hardest-hit country, Indonesia, happened to be ASEAN's *primus inter pares* that has functioned as the positive force for regional stability and the success of regional co-operation. The protracted economic and political crisis in Indonesia clearly absorb much of Jakarta's attention and resources in coping with the immediate impacts of the crisis. For example, the social impacts of the economic crisis present a headache for the government. The International Labour Organization (ILO), for example, estimated that 140 million people will live under the poverty line in 1999 (66 per cent of the population-57 per cent in urban and 72 per cent in rural areas).³⁸ Unemployment is estimated to reach around 6.2 million people in 1999, and around 35 million people is under employment (working less than 35 hours per month).³⁹ The economy contracted by 13.8 per cent in 1998 and it was estimated that GNP per capita decreased from US\$1,088 to US\$250.⁴⁰ What such situation can do to social and political stability has been demonstrated tragically in May 1998. Under such circumstances, foreign affairs naturally become secondary, if not lower, in the national agenda. Though in varying degree, other ASEAN countries are also facing more or less similar problems. Thailand, which suffered serious economic setback after Indonesia, is now obliged to focus its attention and devote its resources to

the economic recovery efforts. To a lesser degree, Malaysia is also preoccupied with the need to contain the effects of the crisis on domestic politics.

The crisis is bound to have significant impacts on intra-ASEAN relations. Changes in a member state are most likely to have effect not only on another member state, but also on the region as whole. The Indonesian case clearly demonstrates how social and political turmoil in a domestic context has raised regional and even international concerns. For example, economic hardship in Indonesia is believed to have increased the number of illegal migrants reaching to Malaysian borders.⁴¹ It has been warned that "bilateral friction between Indonesia and its neighbours could also increase in the years ahead if domestic economic and social conditions continue to deteriorate and massive numbers of Indonesians pour particularly into Malaysia and strong preventive measures are taken."⁴² On the other hand, forced repatriation by Malaysian authorities and severe measures leading to several deaths at detention camp prompted Indonesia to claim human rights violation.⁴³

There has been growing concerns also over the projection of domestic ideas onto regional domain, either by government or national NGOs, that might open up new sources of bilateral conflicts. There are some indications that the push for democratization and respect for human rights initiated by national NGOs begins to move beyond national borders. Some NGOs based in Thailand, the Philippines, Indonesia and Malaysia, for example, have begun to exert pressures on Myanmar government

over democratization and human rights issues in the country. Stable relationship between Malaysia and Indonesia has also been affected by growing concerns on the part of Indonesia's NGOs over domestic political developments in Malaysia in the wake of the arrest of former Deputy Prime Minister Anwar Ibrahim. As democratization process in a number of ASEAN countries is becoming more consolidated, it will increasingly become more difficult for governments of those countries to prevent such "intrusion" into "domestic affairs" by their respective NGOs. This trend, consequently, will increase the possibility of more friction among ASEAN member states.

Beyond ASEAN, the crisis and its attendant impacts on individual member states and on ASEAN as a group then raises doubts over the ability of the Association to maintain its role as a manager of regional order in the wider Asia Pacific region through its central role in the ARF. For more than two decades, ASEAN's credibility as a regional organization had been based on the achievements made by core member states in economic development. Now, after that economic achievements have been shattered by prolonged regional crisis, ASEAN's credibility has also been questioned. It has been argued, for example, "the economic crisis may well make the Association more distracted, inward-looking and less cohesive. Long-standing rivalries within ASEAN may resurface ..."⁴⁴ Indeed, the immediate impact of the crisis has been a much weakened ASEAN due to member states' preoccupation with their respective internal affairs. The crisis demonstrates how external commitment was easily strained, if not diverted,

by more pressing issues in the domestic front. Concerns over the lack of leadership within the Association has already been voiced by key members of ASEAN such as Singapore.⁴⁵ Therefore, ASEAN is now faced with a number of internal challenges that might compromise its international standing in the eyes of non-ASEAN members of the ARF, especially the major powers.

Challenges From the Major Powers: China and the United States

Challenges to ASEAN's leadership in the ARF has not only resulted from the Association own internal weaknesses in the face of the crisis, but also come from other sources outside ASEAN. In this regard, there are three significant aspects of this "external" challenges that need to be taken into account by ASEAN if it intends to retain its current position in the driving seat. *First*, there is a problem of different motives among the major powers that guide their respective approach and attitude towards the ARF. Unlike ASEAN countries which see their membership in the Association as an essential part of their national interests, the prime motive behind the willingness of ARF members to participate in the Forum, especially those of the major powers, has been diverse. It has been argued, for example, that "the formation of the ARF was ASEAN's way of trying to stay at the centre of regional security dialogue"⁴⁶ because it feared that "it risked being marginalized and replaced as the preeminent international organization in Asia."⁴⁷ Meanwhile, it has been noted that the ARF "offered China a chance

to question the US leadership role in the Asia Pacific region, to prevent Japan from assuming a military role, to provide a forum to refute the theory of 'China threat.'"⁴⁸ For its part, Japan supported the ARF in the hope that it could create "a new structure of regional relations that would perpetuate US military engagement."⁴⁹ Converging these different motives into one that puts regional security above narrow strategic interests of individual state is not an easy task to be undertaken by ASEAN.

Second, there is what may be termed as the challenge of the "China factor." China's position and role in the ARF often creates a sense of frustration and poses a dilemma for ASEAN. On the one hand, ASEAN tacitly expects the ARF to serve as a vehicle through which China's positive engagement in a region-wide multilateral security dialogue can be assured. For ASEAN member countries, an ARF without China's full participation would be meaningless. On the other hand, ASEAN has made it clear that it intended to undertake the "obligation to be the primary driving force of the ARF." However, there is a limit that ASEAN has to face in undertaking that role. The absence of critical issues to regional security and stability such as Taiwan and the South China Sea on the agenda of the ARF, for example, demonstrates the limited capacity of this forum (and ASEAN) to undertake such a role. The choice for ASEAN is really limited. To accord more importance to China's participation in the ARF would provide a greater opportunity for China to exploit its "special" place in the forum to its advantage. This, in turn, would weaken ASEAN's claim to become the "primary

driving force." However, if ASEAN forces its way to assert that role, this would entail the risk of hampering the ARF process. A more assertive ASEAN's attitude towards China might be seen by Beijing as an attempt to entertain the idea of "ganging up against China."

Finally, there is a problem of dealing with the growing US challenge to ASEAN's leadership in the ARF and its measured support for multilateralism. The US has always criticized the ARF for its lack of ability to address core regional security issues such as the Korean Peninsula and Taiwan. Moreover, Washington has not considered ARF's progresses in overcoming mutual suspicion among states to be impressive ones.⁵⁰ This explains why the US continues to put a higher priority for bilateralism in its approach to regional security. And, "by implication, US bilateralism puts ASEAN's central role in regional multilateralism under increasing pressure."⁵¹ Indeed, it has been noted that "Washington has evidently decided that the key multilateral elements of a new regional order should be really organized by the great powers, and that, if there is any lasting proprietary role, it should be played by the United States."⁵² When the limits of the "ASEAN way" -- as the core organizing principle of the ARF process -- was further exposed by the outbreak of the economic crisis, ASEAN's intention to retain its exclusive managerial role has been further weakened.

The Limits of the "ASEAN Way"

It is unfortunate that the economic crisis, and its attendant impacts on ASEAN,

has heightened some doubts over the effectiveness of the Association's leadership. More specifically, the crisis reinforces doubts over the Association's ability to administer and ensure the relevance of the ARF process for non-ASEAN members in particular and for the entire region in general. However, such doubts are not new because they have been raised even long before the crisis. In fact, there is a growing body of criticisms that pose an even more fundamental question to the nature of ARF as an extended model of ASEAN approach to regional security. At issue here is not so much the resentment against ASEAN's position as the primary driving force, but more on the applicability of the so-called "ASEAN Way" into ARF. In terms of its relevance, this line of criticisms of ARF, and ASEAN's role in it, seems to have more merits and, therefore, deserves more attention.

There are at least five aspects of "the ASEAN way" often seen as the impediments to the ARF process: its principles, context, the nature of ASEAN's approach to conflict, its limited ability to contribute to peace process in Northeast Asia, and the Association's trepidation with things Western. *First*, it is argued that the principles that have worked within the ASEAN context might not necessarily work for the wider Asia Pacific region. For example, it has been argued that the ASEAN model stalls when it is implemented into ARF because the Association believes that "inclusivity and unanimity are desirable and feasible on the most important issues of Asian security."⁵³ ASEAN's emphasis on the gradual process and consensus-building is also seen as a problem for the ARF

because "it will appear irrelevant, should it become bogged down in preliminary CBM discussion without ever tackling serious conflicts of interests or threatening behaviour."⁵⁴

Second, the context in which ASEAN developed differs significantly from that of the ARF. It is argued that "ASEAN countries' status as weak states in an inhospitable environment provided the incentive for them to co-operate. ARF, by contrast, has many powerful states as members and is not unified by the perception of common external threat."⁵⁵ In order to succeed, consensual and procedural approaches requires strong commitments from all parties -- both major and lesser powers -- to abide by rules of the game. However, in the case of ARF, efforts to extend "the ASEAN way" into the process "are doomed to failure as long as China refuses to respect the interests of others."⁵⁶ In other words, the ARF is seen as an organization which does not possess the leverage to restrain major powers' tendency to pursue their own interests contradictory to the ARF's goals and objectives.

Third, ASEAN's experience in dealing with conflicts, which prefers conflict-management and conflict-avoidance over conflict resolution, is not sufficient to address current security problems in the Asia Pacific. Therefore, since "its ability to reconcile conflicting objectives or resolve contentious relations of states is extremely limited...", then "ASEAN can offer little guidance to ARF in how to address and resolve conflicts between its member states."⁵⁷ The ASEAN model has also been criticized for its conviction that "the

most difficult issues should be deferred until easier ones are settled."⁵⁸ This directly points to the limits that ASEAN might face if the ARF process is to proceed to the third stage. Therefore, it is not immediately clear how ASEAN can drive the ARF to undertake the task of elaborating approaches to conflict resolution. In other words, it can be argued also that ASEAN will not be in a position to lead the ARF process into the third stage "precisely because it has declined to develop effective conflict resolution mechanism for itself."⁵⁹

Four, there is a problem of ASEAN's limited capacity and authority to address and contribute positively and effectively to security problems in Northeast Asia. While it is certainly true that the establishment of the ARF by ASEAN reflected the Association's greater appreciation of the interrelationship between Southeast and Northeast Asian security, there are evidence to argue that ASEAN in fact has not demonstrated sufficient interest in promoting Northeast Asian security problems into the ARF agenda. For their part, Northeast Asian countries feel that their problems are ignored.⁶⁰ Moreover, ASEAN's insistence to extend "the ASEAN way" to Northeast Asia has been cited as an example of ASEAN's insensitivity to the nature of security problems in that sub-region. Therefore, due to its uncertain contribution to Northeast Asian security, ASEAN's leadership in the ARF "can do little to promote security" because "North Asia and not Southeast Asia is the locus of regional strategic tension."⁶¹

Finally, ASEAN's approach to multilateral security, which dismisses the European model as irrelevant, has been critic-

ized as an attitude that defies reality and "precludes creative approaches to specific problems."⁶² Meanwhile, the diversity of security conceptions and experiences among member states, which consist of both "Asian" and "Western" powers, requires "flexible, pragmatic approach that emphasizes near-term solutions to hard problems."⁶³ In this regard, the notion of uniqueness strongly upheld by some ASEAN members -- what has worked in one area will not necessarily work in other area -- appears discriminatory. In resisting the proposal made by Australia and Canada that a CSCE model can be adapted for Asia, for example, Indonesia's Foreign Minister Ali Alatas warned that "we have to be careful not to think that certain things that work in one region ought to be transplanted to another."⁶⁴ Following this logic, one can also legitimately ask why ASEAN thinks that what has worked among more or less equal partners in Southeast Asia can be transplanted to a grouping of states, a more diverse Asia Pacific region.

Concluding Notes: Responding to the Challenges

Indeed, in light of dramatic changes both in the domestic and external context of many ASEAN member states since the outbreak of economic crisis and its attendant effects on ASEAN as a group, some elements behind the underlying rationale that provided a degree of legitimacy for ASEAN leadership role in the ARF process -- strategic convenience -- began to wane. Despite the fact that an ASEAN-centred ARF did achieve gradual, though

limited, success in fostering the multilateralization of security in the Asia Pacific region, the outbreak of the crisis has pushed the ASEAN model into the limit. As the crisis exposed the limits of ASEAN approach in managing regional security, it perfectly makes a lot of sense to argue that "the strains on the Association will accordingly have a varied impact on its institutional commitments in the Asia Pacific."⁶⁵ It is in this context that the question on the adequacy of ASEAN's role in driving the ARF process, and the need to undertake some adjustments, becomes more relevance and pressing.

In view of the above need, especially due to the current immobility of ASEAN in the face of the crisis the growing impatient among non-ASEAN members, a leadership role to drive the ARF process will no longer be effective to be undertaken by ASEAN alone. That, however, does not necessarily mean that ASEAN should relinquish its chairmanship role to others altogether. Nor does it mean that ASEAN should continue doing business as usual and ignore the need to undertake some adjustments. Similarly, if non-ASEAN members insist that ASEAN drops its claim to be "the primary driving force," it is not immediately clear what advantage it would bring to the ARF. As argued earlier, the title confers only managerial and procedural role for ASEAN in an administrative sense rather than substantive one. Moreover, one aspect of the strategic convenience factor -- ASEAN as an acceptable interlocutor to all -- remains in place.

What are the necessary adjustments that ASEAN should undertake in order

to function better and live up to the expectation of (some of) its members? At least, there are four areas that need greater ASEAN's attention. *First*, there is certainly a need for ASEAN to be more flexible and realistic on the question of its central role in the ARF process. ASEAN should continue to retain its central role in administrative way, but the attempt to move and drive the ARF process could be undertaken, for example, through a co-chairmanship arrangement between an ASEAN and a non-ASEAN member of the ARF.

Second, ASEAN should devise and promote a decision-making mechanism that allows partial agreement and progress to be made. In order to produce more meaningful and concrete progress, ARF should not constrain itself with the principle of unanimity before it can arrive at an agreement. Here, a formula of 22-X can be considered as a useful one. Possible agreement to be reached among those members that are likely to agree on certain issues should not be postponed until all members give their consent. APEC can provide necessary lessons in this regard. For example, the fact that Malaysia objected to the time-table set in the Bogor Declaration of APEC Free Trade Agreement did not preclude other members from committing themselves to the deadline for trade liberalization. Different deadlines for the implementing AFTA agreement among ASEAN member states can also provide some guides. In the ARF context, if there are only five or six member countries that can agree on specific and concrete CBMs or preventive diplomacy measures, then they should be allowed to proceed with it without forcing others to follow.

Third, ASEAN should address the question of credibility. If ASEAN wants to restore its weakened credibility, and thereby regaining its voice in the ARF, members have to be willing to discuss seriously greater ASEAN co-ordination both in security and other matters. Here, it is imperative for ASEAN to strengthen its "internal structures" as a prerequisite for restoring its credibility either as "the manager of Southeast Asian regional order" or as "the primary driving force of the ARF process." Since ASEAN sees the main function of the ARF is to promote stable relationships between regional major powers, its role in making the ARF process meaningful largely depends on the ability of the Association to enhance its own credibility by transforming itself into a more unified, effective, institutionalized, and cohesive organization. It is these internal qualities that provide necessary guarantee to ASEAN's continued leadership in such a region-wide forum, especially in managing the ARF processes: from initial Confidence-Building Measures (CBMs), through Preventive Diplomacy, to the elaboration of approaches to conflict.

Finally, in order to sustain its "primary" role in the ARF, ASEAN should initiate some concrete programmes or actions that would satisfy those who want to see quick results. This is necessary to alleviate the feeling among some members that ARF is in fact no more than a "talk shop" without meaningful actions. Of course, one could always argue that such expectation ignores the fact that the ARF is just a newly-born undertaking and, therefore, it would be unrealistic to hope that it will produce quick results. It may also be true

to say that the ARF has, in fact, registered some progresses. For example, it has agreed to move the process from the initial phase of CBMs to that of Preventive Diplomacy. However, the initiation of more concrete actions is still needed. In this regard, it is only natural to expect that ASEAN will continue to undertake an active role not only in shaping the agenda of the ARF, but also in providing creative suggestions for concrete programme.

In conclusion, it can be said that while it is certainly necessary for ASEAN to remain in the driving seat, it is also important to ensure that such a role is not meant to preclude non-ASEAN states from playing an equally leading role in the ARF. However, the existing *modus operandi* -- incrementalism and gradual approach -- should be maintained. While the ARF certainly needs some adjustment and modification, there is no need yet to establish a new institution. It is important to note that the ARF process as a form of multilateral approach to security is not meant to replace the existing bilateral arrangement. In the Asia Pacific context, institutional approach to security is not yet in the position to replace power politics practices. Its main function is still to create trust and transparency with the ultimate object of reducing, not eliminating, the importance of alliances and military power. Until a visible and viable alternative to the ARF is found, the existing arrangement and process should be maintained. But, it certainly needs necessary adjustments. To that effect, ASEAN is still obliged to balance conservatism on the one hand and the imperative for change on the other.

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Civil Society and Development: The Missing Link*

Hadi Soesastro

Introduction

SOCIETIES in East Asia are in a process of democratization. They are at different stages in the process. Some have been able to establish a vibrant democratic society (Philippines and South Korea), others are at varying degrees of infancy (Thailand, Indonesia since 1998), and some others are still trying to find the best way to opening up their political system (China, Vietnam). Some East Asian countries believe that they have established an Asian-style democratic society (Singapore, Japan?). In other societies formal structures of democracy exist but the conditions for the full realization of democracy are weak or weakening (India, Malaysia?).

The process of democratic consolidation and the nature of democracy that exists in a society are perhaps reflected in the strength of its civil society. Civil society is, together with state and market, one of the three "spheres" that interface in the making of democratic society (UNDP 1993). In the words of Barber (1998), civil society is "an independent domain of free social life where neither governments nor private markets are sovereign." Civil so-

ciety has also been called the private non-profit sector or the voluntary sector. The important, perhaps critical, role of this "third sector" in the democratization process has been advanced by Walzer (1997) in unambiguous terms: "only a democratic state can create a democratic civil society; only a democratic civil society can sustain a democratic state." Wolfe (1991) believes that "both democratic government and a free economy depend on virtues and values generated neither by the state nor by the market, but by civil society."

Civil society can influence resource allocations (Soesastro 1997). More importantly, civil society in East Asia today has acquired significance in the context of both democratic consolidation and improving governance. The latter results from a widespread agreement that the lack of good governance has been one of the main causes of the financial crisis in the region. The crisis has demonstrated also that good governance cannot be separated from political development, namely democratization (Soesastro 1998). The process of democratization in Indonesia has accelerated as a result of the crisis. This process has been sustained by the rise of civil society that has become greatly aware of the importance of good governance. Thus, as Riddell and Bebbington (1995) have sug-

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gested, civil society becomes a code for "a set of ideas related to participation, good governance, human rights, privatization and public sector reform." It becomes a package deal about governance mechanisms, values, and economic forms.

The crisis has helped East Asians discover the role of civil society in the development. Thus far, it has been the "missing link" in the social, political and economic "space" that has been occupied predominantly by the state and the market. The notion of civil society as the third sphere suggests its emancipatory nature. The expansion of civil society is seen as the expansion of the space for moral, power-disinterested action (Diamond 1991). It is the space of "uncoerced human association" (Walzer 1992). Is it, therefore, possible for civil society to help develop harmonious relations between civil society and the state, producing a more "civilized society"? Or are they bound to be in confrontation, or competition, with each other? Does the notion of civil society imply a relationship that works to limit the state's capacity to pervade and control society? Should civil society provide a check on the excesses of the state (and the market)? Should it reign in the state, or should it oppose the state? These are definitely the most salient questions for the East Asian region today. Will civil society-state relations in East Asia be structured largely by "state corporatism" that has already made a deep imprint on state-market relations that are not easily dismantled? Is this likely to result in the creation of a "state-led civil society"? Or, will the region in the post-crisis environment begin to build a new "tripartite" governance model for in-

teractions between the state, market, and civil society? The fundamental question is whether the region can put much confidence on civil society.

Why Civil Society, and How?

In the view of Andrew Norton (1997) the interest in civil society is in part a result of the convergence of two intellectual trends. The *first* is free market liberalism that seeks alternative ways to provide services, including by civil society through non-governmental organizations, because "the government is ineffective in much of what it does." The *second* is communitarianism that seeks to provide an alternative to state-based communities through civil society, by "providing belonging and attachment without coercion." The revival of civil society in America reflects a widespread sense that changes in the society have outpaced the capacity of older forms of civic and associational life to help individuals and communities cope (Dionne 1998). Here, the interest in civil society also reflects a reaction against government (on the part of libertarians) and a desire to rebuild responsive and energetic government (on the part of liberals).

In many societies today internal and external changes have led to a revisiting of the ideas of the relationship between state and society. The North-South Institute of Canada has identified five reasons for the renewed interest in civil society (The North-South Institute, no date). *First*, the dismantling -- or the perception of it -- of the welfare state in the industrialized countries has led to the expectation that the private non-profit sector, will provide the

services. *Second*, concerns about the decline of the social capital, resulting from individualism in developed societies or caused by prolonged state domination in developing societies, have led to the desire to return to community spirit, voluntarism, and association forming. *Third*, the triumph of capitalism and the spread of the free market system, necessitates a civil society that could assure greater equity. *Fourth*, the globalization of democracy leads to the need to foster a "good governance" basket of attributes: formally democratic and administratively efficient practices, in addition to the counter-balancing efforts of civil society. *Fifth*, the collapse of sovereignty leads to the rise in global civil society. In addition to these, perceptions of aid-donor countries or agencies that aid has failed have led to the promotion of civil society in the recipient societies by the donors. Civil society is seen as both an improved channel for aid and an important prerequisite for the termination of aid.

The above suggests that much is being expected of civil society. It serves to promote democratization; in fact, it is seen as a prerequisite for democracy. Diamond (1991) identifies six functions of civil society in shaping democracy: (a) to act as a reservoir of resources to check the power of the state; (b) to ensure that the state is not held captive by a few groups; (c) to supplement the work of political parties in stimulating political participation; (d) to stabilize the state because citizens will have a deeper stake in social order; (e) to act as a locus for recruiting new political leadership; and, (f) to resist authoritarianism.

In addition, it is expected to provide services to the poor and underprivileged

members of the society. In fact, it is also expected to provide for the social safety net in the society. It should help assure sustainability by engaging in capacity building and human resources development. Furthermore, it is expected to facilitate economic liberalization. And finally, it is thwart governments or particular groups or political agenda as well as to send political messages.

It is, thus, legitimate to be concerned that civil society too will be overburdened and overloaded. Therefore, it is important to view civil society in the context of the developmental challenges in the individual societies. Voluntary organizations are by nature somewhat unstructured, they are disparate and atomized. Occasionally they are engaged in coalitions, but most of the time they are fragmented. Is there any need for these organizations to pool resources, or should they remain diversified? Should priorities be set society-wide, or should they be left to individual groups to decide? Is civil society to act mainly as "mediating structures" whose main agenda is to promote social justice, as proposed by Berger and Neuhaus (1996)?

It is likely that the prevailing situation and environment in a society will influence the agenda and activities of organizations and movements as well as networks of organizations that constitute civil society. Both civil society organizations and agencies or foundations supporting the development of civil society have been preoccupied with two issues. The *first* is on the importance of the enabling environment for civil society to develop. This must rest on a belief in civil liberties. As Blancy and Pasha (1993) have argued, there must be

"a system of rights, constituting human beings as individuals, both as citizens in relation to the state and as legal persons in the economy and the sphere of free association." Above all, civil society must work to put and maintain such a system in place.

The *second* issue is on the need to strengthen the management, funding, and human resources of civil society organizations so that they are able to function effectively. Much attention has been given to the strengthening of non-governmental organizations (NGOs), but civil society includes organizations that are not NGOs in the sense commonly used. Peasants that organize themselves to defend their land rights or to demand for a fair compensation for the land used for development projects are often overlooked.

Two other issues deserve equally serious attention. The first is the need for civil society structures that can absorb and mediate conflict. Civil society is not necessarily a harmonious sphere in which there are no conflicts. According to Giddens (1999), the state should also protect individuals from the conflicts of interest always present in civil society. This has raised an important question about the role of government in promoting civil society: Will the hand of the government necessarily produce state-led civil society?

The second is on the importance of international co-operation among civil society organizations to pool their resources in shaping international (and regional) public policies, which in turn could influence national public policies. Networks of non-governmental organizations are playing an important role in the Asia Pacific region

in shaping policies to promote regional co-operation and confidence building. They have dubbed as the Second Track, because of their interaction with intergovernmental fora (First Track). Examples are: ASEAN ISIS (Institutes of Strategic and International Studies) that interact with the ASEAN Foreign Ministers Meeting (AMM) and the ASEAN Senior Officials Meeting (SOM); there is also PECC (Pacific Economic Co-operation Council) that interacts with APEC, and CSCAP (the Council for Security Co-operation in Asia Pacific) that interacts with the ARF (ASEAN Regional Forum). All these regional non-governmental institutions have been initiated by civil society organizations, including academic institutions. PECC paved the way for the establishment of APEC. ASEAN ISIS promoted the idea of ARF and took the initiative to organize CSCAP as a second track organization for the ARF.

As stated earlier, the weakening of sovereignty has given rise to global civil society. In place of governments civil society organizations are seen to be more representative of the populace. Civil society organizations may also assume the role of international watchdog over the actions of states on the international level. In many instances they also take up issues that are traditionally seen as a domestic issue (e.g., the policies of the military regime in Myanmar, or the problem of East Timor). In Asia Pacific, this has given rise to a growing network of second track institutions. Although these non-governmental activities exist, there is a tendency on the part of governments in the region to create their own state-led civil society at the regional level. Woo (1998) suggested that the involvement of

non-governmental actors in APEC fora has come about mainly as a result of collective state action. He argues that APEC collectively has not been receptive to the voices of the non-state sector except through associations or groups that it has officially sanctioned. He attributed this to such factors as the influence of ASEAN and Japan in the formation of APEC and the belief that the Asian miracle rests on the adoption of the corporatist development model. These factors may no longer hold today. It remains to be seen whether APEC will continue to promote a state-led civil society at the regional level when the development of civil society has gained greater momentum at the national level in many countries in Asia Pacific.

Civil Society and Development in East Asia

The following is a survey of the issues of civil society and development in several East Asian countries. A brief discussion of the developments of civil society in India is included as it may share some common problems with the East Asian countries.

China

According to Wang (1999), there is a lot of rethinking in China today about the relationship between state and society. This has been triggered by the collapse of the communist regimes in the Soviet Union and Eastern Europe as well as by the rapid internal developments within China that take place in all fields. In addition, the attention inside China on civil society has also been influenced by the intensive discus-

sion on the subject internationally as well as due to the rise of NGOs globally.

The debate on civil society in China began only in the early 1990s. It remains theoretical rather than operational, and academic rather than political. The central committee of the Communist Party (CP) has neither condemned it nor approved it, perhaps cautiously recognizing the need for the country to enter into a discussion on the changing nature of the relationship between the state and society. The "third way" is being examined more closely as it may have attractive features for China.

In China there are various interpretations of the term "civil society." It is sometimes used interchangeably with civilized society, civic society, or mass society. Mass society, used originally in the Chinese language in Taiwan, has the connotation of grassroots (people's) power and implies an opposition to the state by the society. Civic society is a concept that emphasized the value of political participation by the citizens. Civilized society implies greater respect for individual and human rights and the rule of law. It is the latter interpretation that has received widespread support in China. It is also understood that the middle class plays an important role in the development of civil society as the middle class function as the bridge or as "mediator" between the state and the public (the masses). Intellectuals are seen as being in a very important "mediating" position, and increasingly there is appreciation of the role of intellectuals that are "outside" the system.

Civil society organizations in China have their own "Chinese characteristics" in that they are "half official and half non-

official." This suggests that a state-led civil society is prevalent in China. As Wang described it, the government sometimes uses these organizations as "a sort of channel [for] social control," and the organizations often become powerful through the support of the state. There are views that consider this situation as not necessarily negative. The argument is that an independent civil society never existed in China's history, and civil associations that have played an important role in society have maintained a special, intimate relationship with the government.

Wang argued that the development of civil society in China is a necessity, but it will not emulate that in Western societies. Yet, he pointed to the fact that it will have to take into consideration the demands of the Chinese people today for affluence and happiness, for social security and guarantee, for autonomy and freedom, for equality and justice, and for democratic participation. He noted that the common people can no longer accept the Communist propaganda. Thus far, according to Wang, the impact of these developments in China is felt most in the area of foreign affairs. There is greater interests and support for China's regional and global role as a respected member of the international community. There is now talk about China's "constructive" international role. Academic discussions point to the possibility that the "national interest" as defined by the state may differ from that as understood by the people. New concepts of security have also emerged. It can perhaps be argued that the strengthening of civil society in China may to some significant extent come through its involvement in international affairs.

Indonesia

According to Buchori (1999), civil society is an alien concept in Indonesia. It is not yet well understood until today. In Indonesia the term means *masyarakat madani*. This was originally used in Malaysia and was introduced into Indonesia by Anwar Ibrahim in 1994 during the second Istiqlal Festival in Jakarta. It has been taken from the Arabic word *al-mujtamai al-Madani*, which in the Middle East has been used to convey the idea of civil society. However, this concept purports to include the civilization of the entire society, including the government. Consequently the government has made civil society its business. Presidential Decree No. 18/1999 of 24 February 1999 established a National Reform Team towards *Masyarakat Madani*. There are concerns that through this decree the government is trying to co-opt the existing civil society organizations.

The role of civil society in Indonesia is still weak. The main constraint has been political. The fall of Soeharto opened up a greater space for civil society. Although this has unleashed a democratization process, civil society continues to be seen by the transition government of Habibie as a serious threat to its survival as civil society is at the forefront in the opposition of the Habibie government and its continuation in power. Buchori believes that civil society will survive and gradually develop in Indonesia, but this will be critically influenced by the process of leadership transfer. Hikam (1999) is of the opinion that the role of civil society in Indonesia, as manifested mainly by NGOs, will increase because of the current global and national trends towards debureaucratiza-

tion and decentralization of decision-making processes in society.

Although, as suggested by Buchori, the concept of civil society may be alien to Indonesians, Hikam proposed that NGOs are not a new phenomenon in Indonesia. Many traditional institutions have functioned as "social empowerment agencies." As described by Eldridge (1990), the main role of NGOs in Indonesia is to enhance the capacity for self-management among less advantaged groups, enabling them to deal with government agencies and other powerful forces on more equal terms. A more recent development in Indonesia is marked by the emergence of "issue-oriented NGOs." They have arisen in response to the concentration of power and to "top-down" approach in the development under Soeharto's New Order governments. These issue-oriented NGOs have gained prominence due in part to their efforts to provide alternatives to the society beyond the state's framework and strategy of development.

The active involvement in civil society in the change of government and in the demand for reforms in all fields, including governance, has built up a momentum towards expanding the space for civil society. Civil society has also participated actively in assuring that the recent general elections are conducted fairly and freely. Various election monitoring groups have been set up to prevent a recurrence of the practice of vote rigging by the state apparatus and the government party.

By and large civil society organizations in Indonesia are still weak and have limited capacity. Internally it is because of the lack of managerial and leadership

skills. Externally it is caused by the pressures from the state. But most importantly because they are financially dependent, mostly on resources from external sources.

The Philippines

The guarantee by the state of a space for civil society in development is an important feature in the Philippines. The sphere of civil society participation in governance has widened with the process of democratization that has been unleashed by the overthrow of the Marcos government. A study by Magno (1999) shows that in the environmental sector NGOs have become legitimate players in influencing decision-making at various levels of governance. At the national level, NGOs have various institutional openings. These include the establishment of an NGO desk that addresses NGO participation in the development programmes of the Department of Environment and Natural Resources. There is also NGO representation in the Philippine Council for Sustainable Development that monitors the government's adherence to the environmental agreements reached at the 1992 Rio Summit. Environmental NGOs are also engaged in the implementation of national policies such as the National Integrated Protected Areas System approach to biodiversity conservation. NGOs are given seats in Protected Area Management Boards that are tasked to undertake programme planning and implementation in the respective sites.

At the local level, NGOs are secured to participate in local development councils under the 1991 Local Government Code. Here, NGOs can push for a sustainable development agenda in deliberative processes

with the local government units. In Cagayan de Oro a tripartite arrangement called Task Force Macajalar was formed in the mid-1990s to combat illegal logging. In the province of Misamis Occidental joint government-citizen checkpoints have been set up to prevent transport of illegally-cut timber products from the province. There is widespread realization in the Philippines that environmental management tasks previously undertaken solely by the state are more effectively undertaken through co-operative systems involving government, NGOs, and people's organizations (POs).

Thailand

In Thailand, traditionally the state was very strong and civil society organizations were weak. Student organizations were the first civic groups that fought for democratization and social justice in October 1973. However, as shown by Bunbongkarn (1999), as the economy grew, civil society organizations became stronger and played more effective roles against the state power and the interest of the business community. These organizations have been formed to check the government, the politicians, the bureaucracy and other state mechanisms. As in other countries, most of them represent the interests of the poor, women, children, the underprivileged, and the rural people who are politically and economically weak and are unable to fight for themselves.

As in the case of Indonesia, the crisis has provided greater opportunity to civil society to exert its role in pressing for reforms. The issue of good governance, both public and corporate, is now firmly placed

in the national agenda. This process has begun before the crisis. It was soon realized that the democratization in 1992 had not produced good government in the body politic as well as in the government administration. There was widespread corruption, and political corruption, as well as vote buying, and a serious lack of transparency. The Pro-Democracy group that opposed the military-supported government initiated the call for a new constitution. This initiative failed to garner support from the liberal political parties and the urban middle class.

However, as political corruption became more serious and money politics became more deep-rooted, in late 1996 the National Assembly decided to set up a Constitutional Drafting Assembly (CDA). The CDA was composed of 99 members, 76 of which were representatives of all provinces, and the remaining 23 were selected from amongst political scientists, public law experts and former public service officials. The National Assembly agreed to relinquish its right to draft a new constitution to an autonomous drafting body in response to pressures from civil society. Several civic groups were effective in influencing the drafting. This led to the introduction of several new civil rights and expansion of existing rights and liberties already protected in the previous constitution. The urban middle class was strenuously campaigning for the endorsement of the draft. The new constitution was proclaimed in October 1997. It aims at enhancing the strength of civil society in Thailand in order to consolidate the democracy and to provide a mechanism for checks and balances.

South Korea

NGOs began to develop in South Korea in the early 1960s, but they were mostly service-oriented, providing welfare services or implementing development projects for the poor, and they were mostly supported by foreign aid. Advocacy groups for the promotion of social justice, democracy and human rights began to grow during the authoritarian regime of Park Chung Hee, but they were severely oppressed. The abrupt end of the authoritarian regime in June 1987 opened up the political space for civil society. As pointed by Jung and Kim (1999), this development has been characterized by the emergence of increasingly effective and sophisticated civic groups led by the younger generation. Environmental groups, powerful labor movements such as Hyundai labor unions, civil society organizations such as the Citizen's Coalition for Economic Justice, human rights and women groups became key actors.

This development has aroused attention by scholars and the business community as well as the public at large on the role of NGOs, not only as an alternative provider of public services but also as a vehicle for the realization of new patterns of governance. The financial crisis has reduced the sources of NGO funding while the demand for their services has increased. The government of Kim Dae-jung is believed to be supportive of civil society organizations. Korea's legal and fiscal environment needs further improvements to enable NGOs to grow and become stronger.

Civil society organizations in Korea are now actively engaged in shaping public policy and in strengthening governance. One example is the coalition of 28 civic

and labor groups, including the Citizen's Coalition for Economic Justice, to push for a legislation on guaranteeing people's basic livelihood. This Coalition has established a body to monitor government agencies for budget waste. A leading civic group, the People's Solidarity for Participatory Democracy has successfully pressed Samsung Electronic Co. to increase the quorum of outside directors and to take other measures to increase managerial and decision making transparency.

Korea is in an interesting experiment to develop a new pattern of governance. The vision for a new governance model, as espoused by Jung and Kim, must assure the full involvement of civil society and a strong and balanced partnership between the three sectors, state, market, and civil society. These sectors cannot be separate and hierarchical. Korea's civil society has become strong enough to become an equal partner in governance. The kind of "tri-partite governance" that will evolve may become an attractive model for other East Asian societies.

India

The other big Asian country, India, has seen an upsurge in civil society activities much earlier than China, namely since the late 1970s largely in response to the centralizing tendencies of state structures and to the increasing incompetence of the state in implementing national development programmes. As described by Jayal (1999), India provides a clear case of the significance that is being assigned to civil society in the twin context of broadening and deepening democracy and of rectifying the lack of state capacity for govern-

ance in general and development in particular.

One of the main tasks of civil society in India is to effect a bridging of the gap between democracy in the formal structures of governance and the absence of the necessary conditions for the realization of democracy. The other main task is to overcome the growing crisis of governability in terms of demand overload and the multiple challenges to governance.

Civil society initiatives in India have taken two types, namely a wide variety of social movements (women, tribal people, and lower castes) and the mushrooming of NGOs that are mostly engaged in developmental work. Members of NGOs mostly come from the middle class. As in the case in many East Asian countries, the involvement of members of the middle class in NGOs is largely due to their disillusionment with electoral politics. Political parties are no longer able to channel the aspirations of the people. As described by Jayal, they have been transformed into election-winning machines rather than instruments of democratic social transformation.

Nonetheless, civil society in India today is an intensely conflict-ridden arena. There are struggles for the control of this space between the secularists and the communalists and also struggles over this space by those who seek to access the state through civil society organizations. Thus, civil society in India is regarded as well developed in the sense of opposition to the state, but it is underdeveloped in terms of associational groups.

An equally important point to note is that in a sense the state has acted as a

guarantor of civil society. Since the mid-1980s, as stipulated in the Five Year Development Plan, NGOs, together with the markets, are recognized explicitly as having a role in supplementing the state in development.

A Concluding Note

East Asia has discovered the missing link in development, namely civil society, but it is still a long way to go to make it an equal partner in a kind of tripartite governance for development, as is currently being crafted in Korea.

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Bank Recapitalization Programme: Measure Toward Economic Recovery*

Miranda S. Goeltom

Overview

THE crises hitting Indonesia since mid-1997 had triggered a significant economic downturn. The process of economic stabilization and recovery in Indonesia, unfortunately, faced several obstacles before materialized. To some extent, this relates to the severity of the damage prompted by the crisis that had paralyzed Indonesia's fundamentals, especially the banking system, business sector, and social and political environment. Mounting inflationary pressure along with battered rupiah exchange rate further compounded the deterioration of the economic fundamentals. The threat of hyperinflation was even alarming precipitated by vicious depreciation-inflation spiral following the excessive expansion of money supply. With confidence in the banking system eroded, the financial intermediary function of banks virtually came to a halt, resulting in a sharp fall in production and investment. It ended up with a deep contraction of the entire economy, accompanied by heightened social and political tensions emanating from

massive unemployment and widespread poverty.

To address the crisis, the government pursued a number of policy measures on both the demand and supply sides. On the demand side, the policy focused on resuscitating investment and trade activities and alleviating the negative impact of the crisis on the poor. On the supply side, policies were focussed on structural adjustment in order to rehabilitate the banking and business sectors. Meanwhile, efforts to contain inflationary pressures proceeded with monetary tightening and the easing of supply-side shortages through the extension of programme credit and the rehabilitating of distribution chains.

The banking restructuring programme, as an integral part of the stabilization policy, constitutes as a priority measure for economic recovery, primarily in the real sector. Its success is expected to restore the intermediary role of the banking sector. In addition to the banking restructuring programme, efforts to revive economic activities have to go hand in hand with the corporate restructuring plan, especially debt restructuring, by way of establishing the Indonesian Debt Restructuring Agency (INDRA) and the Jakarta Initiative, as a

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means of accelerating the negotiations between debtors and creditors.

Highlights of the Indonesian Economy

Indonesian economy is currently confronted with four major problems that led to a deepening crisis. These problems include: (1) weak micro-conditions in the banking and corporate sectors and their ramifications for the entire macroeconomic environment; (2) complexity and scale of the problems faced and their implications on the implementation of economic policies; (3) non-conducive sociopolitical condition and security with its implication on business risk; and, (4) unfavourable global economic environment.

The first basic problem is associated with the balance sheet effect.¹ The formidable balance sheet effects in a number of sectors, including banking, have not only curtailed business activity but also produced imbalances in the balance sheet of the monetary and fiscal sectors that in turn jeopardized macroeconomic equilibrium.

The second fundamental problem has been rooted in the complexity and scale of the problems. This high complexity results from the existing weaknesses in micro-economic and institutional fundamentals.

¹The balance sheet effect relates to restraints in economic activity as a result of the aggravation in the financial status of business entities. This effect takes place as sharp increase on the liability side is not matched by a commensurate rise on the asset side, eroding asset value and a drop in earning capacity as compared to expenses. Against this setting, the business sector tends to prioritize financial recovery as opposed to business development.

The fragile fundamentals which were strongly interrelated, include high dependence on short-term external debt, monopolistic economic structure, poor corporate and public governance, inadequate supervision and inconsistent law enforcement. Consequently, efforts to cope with the crisis call for better planning and co-ordinating in order to reduce high cost.

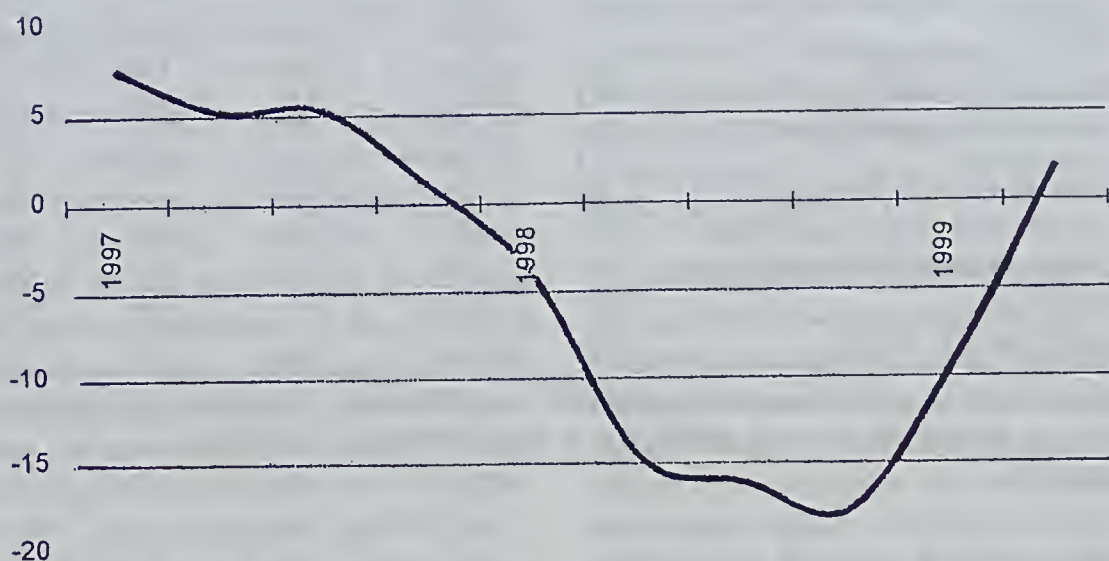
The third problem concerns the high business risk. The high risk could be traced not only from the balance sheet effects but also from non-economic factors, such as inadequate infrastructure and uncertain sociopolitical condition. The high business risk, to a certain extent, had driven domestic investors to transfer their capital abroad. At the same time, the business sector confronted difficulties to regain access to external financing, including trade financing. Against this considerable uncertainty, investment activities have slumped remarkably. Along with the fall of investment there was a dramatic plunge in the utilization of production capacity and workforce.

The fourth problem relates to Indonesia's unfavourable external position. At the time when the external boost was much needed, the global economy, aside from the United States (US), exacerbated the problem, such as the lingering crisis in Japan, turbulence in the international financial market, and the sharp fall in international prices of commodities. This situation precipitated a reversal of capital flows to the US market as a safe haven.

Economic Growth by Sector

As a consequence of the problems cited above, the Indonesian economy encountered

GDP GROWTH



Source: BPS.

ed a severe drop. The sharp contraction in the economy represented a number of contractions in all sectors minus a modest expansion for agriculture sector and electricity, gas, and clean water sector. The non-oil/gas sector contracted by 14.3 per cent, contributing -13.2 per cent to the nationwide economic contraction. Meanwhile, the oil/gas sector also suffered from contraction, primarily as a result of the weakened world demand and fallen oil price in the international market.

Entering 1999, the economic development started to move upward as the contraction slowed down in the first quarter of 1999, and even recorded a positive growth in the second quarter at 1.82 per cent. This benign growth signaled that the economy has bottomed-out, as shown in the graph below.

While only two out of nine sectors recorded a positive growth in 1998, the economic growth in the first two quarters of 1999 showed an auspicious development.

Almost all sectors showed a rebound, except electricity though still recorded a positive growth. Remarkable performance in manufacturing, construction, mining, and services sectors should be given a credit.

Consistency in the implementation of economic policy and positive market sentiment as well as tranquil general election contributed to this development. Rupiah appreciation, easing inflationary pressure and regained investor confidence gave room for business entities to make an expansion. One important aspect is the continuation effort of bank restructuring programme that will provide a strong and sound financial intermediary intensely needed by the economy to recover.

Inflation

The inflation rate in 1998/99, measured by the annual growth of Consumer Price Index (CPI), reached by 45.4 per cent, slightly lower than the percentage target as set

GDP GROWTH BY SECTOR

Sectors	1997	1998	I/99	II/99	1999*
1. Agriculture	1.0	0.8	2.9	7.5	2.8
2. Mining and Quarrying	2.1	-3.1	-1.2	1.5	1.9
3. Manufacturing Industry	5.3	-11.9	-9.4	5.8	-2.6
4. Electricity, Gas and Clean Water	12.4	1.9	0.3	0.1	2.6
5. Construction	7.4	-40.5	-13.2	0.1	-4.6
6. Trade, Hotel and Restaurant	5.8	-18.0	-21.0	-4.3	-1.3
7. Transportation and Communication	7.0	-15.1	-18.0	-1.3	-4.3
8. Finance, Leasing, and Business Service	5.9	-26.6	-23.3	-8.5	-5.1
9. Services	3.6	-3.2	2.4	3.8	-0.8
Gross Domestic Product	4.7	-13.2	-9.4	1.8	-1.2

*Forecast based on data up to first quarter 1999. Central Bureau of Statistic have just recently released the forecast for economic growth that is more optimistic, at 0.1 per cent.

Source: BPS.

by the government, i.e. 45.9 per cent. The high inflation rate occurred in the first half of the fiscal year. Meanwhile, the inflation rate in 1998 amounted to 77.6 per cent, lower than the government's target, i.e. 80.0 per cent.

The risk of hyperinflation loomed, hanging over the Indonesian economy in the first half of 1998/99 as inflation rate reached by 38.0 per cent, far higher than 3.5 per cent in the previous year. The exchange rate depreciation had given rise to sizeable pass-through effect that in turn propelled prices across the broad spectrum. Meanwhile, there had been the inadequacy of supplied goods resulting from a lower level of production, harvest failure, and interruptions in the distribution function. In addition, aggressive monetary expansion contributed in a major way to the bursts of inflation during the period.

In line with the rehabilitation in the distribution systems to channel essential items and the re-established control of the monetary aggregates, inflationary pressures be-

gan to abate in the second half of the reporting year. Inflation fell sharply from a monthly rate of 3.7 per cent in September 1998 to -0.3 per cent in October 1998, marking the emergence of deflation. In the next several months, the inflation rate happened to increase mainly because of seasonal factors. At a later stage, inflation translated again into deflation.

A series of deflation continued to happen from March up to August 1999, totaling 0.71 per cent (year to date), far lower than 46.6 per cent stated in the same period a year before. This favourable development, in line with the positive GDP growth in the second quarter of 1999 gave a significant signal of recovery.

Employment

With deepening contractions in the economy, the unemployment rate increased substantially. In the meantime, real regional minimum wages dropped as a result of the rising inflation. The open unemployment figure, which stated at 4.3 million in 1997,

climbed to 5.1 million in 1998, equal to 5.5 per cent of the total labour force.

Manufacturing industry laid off workers most frequently, amounting to 1.3 million. The other 0.7 million workers lost their jobs in the construction sector, since many construction projects were rescheduled or cancelled. The finance sector also introduced lingering lay off, particularly in the banking industry in consequence of the closure of a number of banks, added to the number of intellectual job seekers. Meanwhile, the labour force in agriculture grew, with the absorption of an additional of 3.6 million workers. This employment growth was in line with the larger role that agriculture played as a resilient basis of the economy in the midst of its crisis.

In line with the population growth, the size of the labour force also grew in 1998 by 1.5 per cent to 92.7 million, as compared with that in the earlier year. It included the stock of previously unemployed workers, the newly laid off workers, and new labour force entrants. The excess supply of labour had caused job seekers to take ill-paying jobs, which did not meet their respective aspirations.

Banking Sector Development

Banking industry is one of the sectors hardest hit by the crisis and remained under downward pressure. Its rehabilitation proceeded slowly because of the complexity and scale of problems as a result of the severe balance sheet effects in the banking industry and a large number of non-performing banks. As such, the banking restructuring programme entailed a lengthy

and intricate preparation, good co-ordination, and enormous costs. The frail banking structure as a result of internal deficiencies was exacerbated by adverse external forces, such as exchange rate turbulence, high interest rates, social and political uncertainty, and a wide range of negative rumors that triggered *bank runs*.

The depreciation of rupiah, followed by the rise of interest rates due to policy tightening to stabilize prices and the exchange rate have led banks to face a negative net interest margin. The negative spread caused further losses and reductions of bank equity capital. The high interest rate environment interrupted the intermediary function of the banks as they experienced onerous difficulties in extending credit.

Settlement of the banking problems had to initially address the structural internal deficiency. The low level of competence and integrity of bank management resulted in poor risk management as highlighted by numerous violations of prudential principles, high-risk investments, and imprudent funding strategy. Added to these internal weaknesses was an emphatically inadequate internal control. Accordingly, banks' performance was in a shambles as reflected in their unbalanced balance sheet in both the asset and liability sides.

On the asset side, the primary problem centered on the deteriorating quality of productive assets. This problem originated from credit lending that was not based on sound lending criteria. Excessive credits were extended to certain groups and banks' subsidiaries in the form of connected lending that resulted in numerous violations of the legal lending limit. Another major

problem came from a large portion of lending to high-risk sectors, most notably the property.

On the liability side, the main problem was a mismatch of currency and maturity where short-term unhedged foreign loans were used to finance long-term rupiah-denominated projects. In addition, the negative spread during the reporting period magnified the substantial loss from the mismatch and introduced a larger retained loss in the thin equity base of the banks. Consequently, banks became considerably more susceptible to disruptive changes.

The internal deficiency in the banking industry was also associated with ineffective supervision of banks. There were five constraints that formed the ineffectual bank supervision. *First*, insufficient number of supervisors. *Second*, inadequate early warning systems. *Third*, a conflicting dilemma between consistent implementation of the regulations and concerns over a probable systemic failure. *Fourth*, the absence of standard operating procedures to exercise an exit policy (a policy that describes ways for any bank to exit from the banking system) that had in fact resulted in moral hazard. *Fifth*, frequent interference from connected parties that hindered any policy remedy from materializing.

In view of the formidable problem, measures in the banking industry focused on efforts to rehabilitate its soundness, clean up its system, and prevent such a crisis from recurring. To restore public confidence, the government issued the blanket guarantee scheme to ensure the security of the bank's liability side. The measures were supported by a monetary policy tightening that

led to high interest rates to absorb excess liquidity into the banking system. To clean up the banking system, the government initiated the bank-restructuring programme, principally through its recapitalization plan. The measures all together managed to arrest the banking crisis. Since the middle of the previous fiscal year, bank runs have subsided and funds mobilized from the public have been flowing in. Nevertheless, the banking industry remained off-track. Bank equity continued to dwindle as a result of continuing current operating losses. The losses centered on rising non-performing loans that consistently swelled the provision for loan losses. In addition, the negative interest spread added to the losses that narrowed the equity base.

Bank Restructuring Policies

In rehabilitating the soundness of the banking system and enhancing its resilience, as well as precluding the recurrence of *bank runs* in the future, the government implemented bank-restructuring programme. The programme rests on four pillars of policy, namely: (1) measures to restructure banks, primarily through recapitalization programme; (2) measures to fix internal conditions; (3) measures to improve bank regulations and law enforcement; and (4) measures to strengthen supervision function.

The first pillar is the most essential ingredient of bank restructuring programme that aims at reinvigorating a credible national banking industry. The programme is directed at restoring banks solvency and profitability so as to enable the resumption of lending. The improvement of bank solvency proceeds with credit restructuring and

transfer of non-performing loans to the Assets Management Unit (AMU) under the Indonesian Bank Restructuring Agency (IBRA) on the asset side, and a recapitalization programme on the liability side. Meanwhile, the restoration of profitability involves three strategies: easing conditions for debtors to settle their debts, facilitating banks that have been restructured and are considered viable, and creating a conducive economic environment for business and banking.

Improvements in bank solvency, brought about by the adoption of the actions under the *first* pillar of the government's programme, do not suffice to prevent the recurrence of the crisis in the future. Therefore, the other three pillars were erected to enhance resilience of the banking system against internal and external shocks.

The *second* pillar covers revisions of the old regulations, such as capital adequacy ratio (CAR) and legal lending limits (LLL), and the introduction of new regulations such as credit restructuring.

The *third* pillar aims at ensuring law enforcement, enacted under Act No. 10 of 1998 that incorporates substantial changes of Act No. 7 of 1992 on banking. The contents of the new law are focused on a shift of authority to issue licences of banks from the Ministry of Finance to Bank Indonesia, elimination of restrictions on foreign investors to own banks in Indonesia, a narrower definition of bank secrecy, and development of *syariah* banks (profit-sharing Islamic banks).

The *fourth* pillar concerns internal consolidation of Bank Indonesia, more consistent rule enforcement, and changes in bank

supervision from regulatory authority to supervisory authority.

Bank Recapitalization Programme

One of the government measures in the bank-restructuring programme is bank recapitalization that covers all banks, including banks under IBRA supervision, except joint banks and foreign bank offices. This programme is intended to bring both the banking industry and individual banks back to their soundness so that they are able to maximize their contribution to the national economy. On the banking side, this programme is designed to sustain banks that have viable prospects to continue to operate and grow, particularly in the course of accelerating progress in economic recovery through ownership restructuring. The bank recapitalization programme was initiated to deal with deficiency of capital that most banks faced. The essential components of the programme are described as follows:

Bank Selection Programme

As an initial selection step, the government classifies banks into three categories, namely A, B, and C, based on their respective capital adequacy ratio (CAR) resulting from the due diligence focused on capital and productive assets. The due diligence involved international auditors.

Banks of A category (CAR of 4 per cent or more) are not required to participate in the recapitalization programme but they have to prepare their business plans. Banks of B category (CAR between 4 per cent to -25 per cent) are required to participate in

the recapitalization programme as long as they meet certain criteria such as fulfillment of the fit and proper test and submission of business plan to Bank Indonesia within one month. Meanwhile, banks of C category (CAR less than -25 per cent) have 30 days to add to their equity base or improve their productive asset quality to the level of B category to meet the criteria for inclusion in the recapitalization programme.

Assessment on Business Plan and Fulfillment of Fit and Proper Test

Research and assessment on the business plan are gradually conducted by the Technical Committee, Evaluation Committee, and Policy Committee, which cover the assessment on the main criteria and additional criteria. The work plan will be classified satisfactory if all components of the main criteria are fulfilled.

Non-performing Loan Settlement

The transferred bad debt recovery has to be used to replace part or all of the government equity in the banks. The government can divest part or all of its equity stocks in bank in the following ways:

- a. Within three years up to the year 2001, bank shareholders can repurchase stocks owned by the government with a call option.
- b. Proceeds from collection of credit that has been submitted to AMU-IBRA should be used to repurchase/reduce government equity in the bank.
- c. After the year 2001, the government can sell its remaining equity stocks to the

public after first of all offering them to bank shareholders.

Resolution of Banks Non-Eligible for Recapitalization Programme

By considering the financial conditions, office network, human resources, and business development, the Evaluation Committee assesses several alternative courses of actions:

- a. bank of B category that is not recommended to participate in the recapitalization programme;
- b. bank unable to fulfill its obligation in the Commercial Bank Recapitalization Programme; and
- c. bank of C category that is unable to increase its capital and therefore it cannot be classified into B category.

Based on the assessment, the Steering Committee can merge the bank with banks of B category or A category, provided that the merged bank is at least included in B category that meet the recapitalization requirement. However, if the merger cannot be accomplished, the Steering Committee will lift the bank business license and liquidate it with or without previously freezing its operations.

Monitoring of Banks Participating in Recapitalization Programme

Close and continuous supervision is required to ensure the effective implementation of the recapitalization programme. This supervision will be done by three parties, namely the compliance director, Bank Indonesia supervisor, and the Evaluation Committee.

The Progress of The Recapitalization Programme

Banking Recapitalization and Restructuring

Based on the result of the due diligence conducted by Bank Indonesia together with International Auditors, and having scrutinized the fulfillment of recapitalization requirements, Bank Indonesia has decided to freeze 38 banks, take over 8 banks, and recapitalize 8 banks.

Indeed, Banking sector recapitalization has entered a decisive stage. The implementation of the banking reform strategy is moving ahead in four major areas -- namely state bank resolution; private bank recapitalization; resolution of banks under IBRA (Indonesian Bank Restructuring Agency); and improvement of the legal, regulatory, and supervisory framework. Bank Mandiri (a merger of BDN, Bank Exim, BAPINDO and BBD) which will receive Rp 137.6 trillion of government recapitalization bonds has formally started to operate by the end of July 1999. The other state banks, Bank Negara Indonesia, Bank Rakyat Indonesia, and Bank Tabungan Negara, are being assessed by an inter-departmental committee to prepare a comprehensive restructuring plan.

The issuance of Government bond in May 1999 indicated that the recapitalization process for the eight eligible private banks has been technically completed. Bank Indonesia is also expected to complete its review and discussion of individual bank's financial soundness and business plans. Corrective programme to deal with non-viable business plans will be established,

when necessary, with individual banks by 30 September 1999. Through this process, and regular supervision, Bank Indonesia will ensure that private banks remain solvent. Meanwhile, the recapitalization of 15 joint venture banks is performed by the bank shareholders, particularly their foreign shareholders.

IBRA will merge eight banks taken over (BTO) by the Government into Bank Danamon by the end of this year. The mergers exclude the bigger banks, namely Bank Niaga and BCA. The eight banks that will be merged with Bank Danamon are Bank Tiara, Bank PDFCI, Bank Duta, Bank Nusa Nasional, Bank Tamara, Bank Pos Nusantara, Jaya Bank Internasional, and Bank Rama.

Another big bank taken over temporarily by the government is Bank Niaga which is still in the process of negotiating with foreign investors to help finance its recapitalization programme, while BCA will be merged with Bank RSI since both banks were under the ownership of similar business group.

The IBRA plans to list BCA late this year or early next year. As part of its drive to raise at least Rp 17 trillion (\$2.53 billion) for supporting the state budget during the year ending 31 March 2000. In addition, IBRA plans to sell a 2.5 per cent stake in PT Indofood Sukses Makmur, a 44 per cent stake in PT Astra International, and an 8 per cent stake in First Pacific Co.

Furthermore, IBRA plans to sell its assets and therefore expects to raise Rp 1.5 trillion between July and September 1999, Rp 4 trillion between October and December, and Rp 12.3 trillion in the first quarter of 2000. A principal focus continues to be

on loan collection and asset recovery by the state banks and, crucially, by the IBRA whose portfolio accounts to be resolved (consisting 12 BTO banks, its Asset Management Investments/AMI for shareholder equity assets, and its Asset Management Credit/AMC for transferred loans).

All state and IBRA banks, and the AMC, have publicized the names of their largest debtors (over Rp 50 billion), initiated restructuring negotiations, established loan recovery units, and set monthly recovery targets through December 1999. All state banks, and IBRA's AMC and AMI have appointed international banks or advisers to assist their restructuring and loan recovery programme. The major BTO banks are also in the process of engaging international banks to assist with restructuring plans and loan recovery management.

As of late June 1999, 784 debtors (accounting for over half of all debtors with loan values above Rp 50 billion) have signed letters of commitment to: (1) full disclosure; (2) co-operation with due diligence audits; (3) a time for concluding restructuring; and (4) willingness to accept a strategic investor or management changes.

On the basis of these letters of commitment, and other preparatory work, all debtors with loan values exceeding Rp 50 billion are being classified under four categories (A to D), depending on their willingness to co-operate and financial viability. Non-cooperating debtors (C-D) categories will be publicized by 31 August 1999 for all state banks, BTO banks, and the AMC; they will be subject to penalties, including prompt filings for bankruptcy and foreclosure, within one month of publication.

Cost of Recapitalization

The cost of the recapitalization programme will be significant. It is now estimated at approximately Rp 550 trillion. To finance the cost of bank recapitalization, the Government has issued government bonds on 28 May 1999. The total value of bonds issued is Rp 157.6 trillion which covers recapitalization programme for 11 private banks and 12 regional development banks, and to cover the government liabilities to Bank Indonesia arising from the guarantee programme during 1998 and 1999. As for the state banks (Bank Mandiri, BRI, BNI, and BTN) and banks which have been taken over in 1999, the bonds will be issued in phases in line with progress made in the restructurization of these banks.

The bonds were divided into three categories: (1) variable rate bonds (VRB), valued at Rp 95.1 trillion with quarterly coupon payment equivalent to interest rate on 3 month-Certificate of Bank Indonesia (SBIs). In this phase the bond issued consists of 16 series maturing within 3 to 10 years. This kind of bond is designed to cover the negative capital of banks, enabling them to reach CAR of zero per cent; (2) fixed rate bonds (FRB), valued at Rp 8.7 trillion with a half yearly coupon payments. At present, two series of the fixed rate bonds have been issued, with a maturity of 5 and 10 years, carrying interest rates of 12 per cent and 14 per cent, respectively. This kind of bond is designed to increase CAR of banks from zero to 4 per cent; and (3) inflation index bonds, which will be periodically adjusted to the CPI (indexed bonds), valued at Rp 53.8 trillion, carrying real interest rate of 3 per cent. This kind of bond is designed to cover the govern-

ment's liabilities to Bank Indonesia, arising from the guarantee programme.

In the current fiscal year, the cost of bonds' interest rate is estimated to reach Rp 34 trillion. The IBRA is responsible for half of this amount. The burden to the state budget could decrease if IBRA succeeded in recovering a large portion (Rp 230 trillion) of its assets the Agency took over from the closed and nationalized banks.

The IBRA has currently controlled roughly 200 companies pledged last year by owners of closed and nationalized banks to repay some Rp 100 trillion in debt to the government. The Agency would attempt to increase the value of the various companies surrendered by indebted bank owners in order to increase its revenue from the sale of the assets.

The Government also expects to recover its investment in recapitalized banks by increasing the market value of the banks through various measures, including management reshuffles. Another source of revenues would be from the restructuring of collateral assets of bad loans currently managed by IBRA.

It is important to understand that while bank recapitalization is necessary in the Short Run to prevent the systemic collapse of the banking system, the fact that government now owns 12 more banks that counts for 75 per cent of the total liabilities of the banking system and about 90 per cent of its negative net worth, makes it very clear that this is neither desirable nor healthy for the long run development of a sound and efficient banking system. Therefore, the overarching imperative that would shape the next phase of the bank

restructuring programme is the restructuring of the state banks and restoring the role of private sector in banking system. Hence, it is very important to watch the development of the dilution of state ownership as planned within three to five years time.

Improvement of the Legal, Regulatory, and Supervisory Framework

In line with the bank restructuring agenda, amendment of the banking law was approved by the Parliament on 16 October 1998. These new amendments strengthened the legal power of IBRA and the AMU. In addition, a new Central Bank law, which provides a greater independence for central bank (Bank Indonesia), was approved by the Parliament, and being implemented since 17 May 1999. Furthermore, a law covering foreign exchange movements and the exchange rate system was also approved by the Parliament; this bill allows Bank Indonesia to monitor capital flows and to implement the exchange rate system adopted by the Government.

In addition, Bank Indonesia has issued a regulation tightening the Net Open Position (NOP) in the wake of volatile currency markets. The NOP is set at a maximum of 20 per cent of a bank's capital based on a calculation consolidating all of the bank's offices both inside the country and overseas. The maximum NOP was set at 25 per cent previously.

Also, Bank Indonesia has temporarily eased the Legal Lending Limit (LLL) rule that allows banks to extend credits to non-affiliated parties up to a maximum of 30 per cent of a bank's capital from the 20 per cent previously. This only applies to

credit extended between 31 December 1998 and 31 December 2001. For the period of 31 December 2001 to 31 December 2002, banks will only be allowed to extend credits up to a maximum of 25 per cent. Afterwards, the LLL will be brought back to its original level of 20 per cent.

Recently, Bank Indonesia has issued new banking regulations as follow-up regulation of the new Banking Act. In general the new regulations cover regulation on capital requirements for new banks, ownership, management, foreign bank branches, *Syariah* banks (Profit sharing Islamic bank), coverage of rural credit banks, mergers, consolidation, acquisition, and liquidation of banks. New private banks are required to have a paid-up capital of Rp 3 trillion. Meanwhile, the capital requirements for rural credit banks are differentiated as follows: (a) in the Jakarta and its vicinity area such banks are required to have a paid-up capital of Rp 2 billion; (b) banks in provincial capitals are required to have a paid-up capital of Rp 1 billion; (c) in other area they are required to have a paid-up capital of Rp 500 million.

As regards to foreign investors, they are now allowed to have shares of commercial banks virtually up to 99 per cent. Furthermore, the new regulations also allow foreign banks to open new branches as long as their assets are among the 200 largest such international banks and they are rated A or better internationally. The new regulations also require a fit and proper test for the owners and management of banks to prevent bank fraud.

In addition, government has undertaken steps to strengthen the oversight role and

functioning of IBRA's Independent Review Committee (IRC): (1) a Presidential decree has been formally issued in establishing this Committee; (2) a new chairman has been appointed; and, (3) a permanent secretariat will be established on site at IBRA, by the end of August, followed by regular meeting of the committee. To ensure transparency and communicate the Committee's findings to the public, the IRC will issue a communique after each quarterly review meeting.

Challenges

It is envisaged that the biggest challenge confronted by Indonesia is to accelerate the process of economic recovery by means of strengthening the effectiveness of both microeconomic and macroeconomic management. The longer the resolution process, the harder the efforts will have to be to escape from the crisis. Given the tremendous balance sheet effects in the country, every delay only raises costs. In addition to enormous material loss, a slow recovery process may heighten the threat of social disorder.

In the monetary sector, the challenge is to strengthen stability of prices and the exchange rates, which started to gain ground. The success in restoring monetary stability will allow an ample room for interest rate declines required for the economic recovery to proceed rapidly. On the contrary, failure in holding monetary stability will jeopardize all gains attained so far.

In the banking sector, the central challenge is to speed up bank restructuring process that is heavily dependent upon the

success in implementing the recapitalization agenda. The restructuring process *per se* aims at preventing a recurrence of crisis. The success in addressing bank crisis is expected to restore the financial intermediary function of banks. The sector's restoration helps to accelerate recovery in the real sector and to prepare the national banking industry to compete in the globalization era.

The bank restructuring programme will focus on three main areas. *First*, the issuance of remaining bonds to finance the restructuring. So far, the Government has already issued bonds totaling more than half of the fund needed for banking recapitalization programme. The fact that interest rate is declining will ease the Government effort to cope with the remaining fund needed, that is estimated roughly Rp 500 trillion (higher than March 1999 figure). The declining interest rate will also give room for banks to overcome the problem of negative spread and theoretically regained its intermediary functions. However, the success of bank restructuring to enhance the economic recovery depends very much on the success of a comprehensive corporate restructuring. This could be achieved not only by way of restructuring debt repayment, but also by means of providing a sound and more competitive business environment.

Second, further measures towards recapitalizing state banks. Bank Mandiri has made significant progress in implementing its restructuring plan and will legally merge its four bank components on 31 July 1999. The capitalization of Bank Mandiri will be done as follows: some Rp 80 trillion of loss asset will be transferred to IBRA at the

legal merger and the remaining 30 trillion will be set at the end of September and December, and be conditional upon achievement of performance objective.

Other state banks are still under preparation of business plan and loan recoveries management, which are conducted by international banks or advisors. BNI is set to be allowed to operate in a commercial manner and be self-standing. BRI is aimed to focus on its core activities of micro-finance, retail, and small and medium size business enterprises. BTN is prepared to focus on its core activity of providing low cost housing finance.

Third, the continuing process of enhancing loan collection and asset recovery will help to boost the bank revitalization. The programme, which initially focused on large debtors, move progressively to those of smaller size. So far AMU/IBRA and most of the state bank have categorized debtors on the basis of corporation and business viability, publicized the name of the largest debtor, and begun the process of negotiation. Progress has also been made in pursuing settlements with the former owners of failed banks that had prudential violations. In order to accelerate the process, some strategies will be implemented, among others are reactivating the role of interagency debt committee and assuring transparency and uniform treatment across debtors.

The authorities have been committed to undertake a review in the second half of 1999 of laws and regulations pertaining to the banking sector. Bank Indonesia supervision department has recently prepared for the frank paper highlighting the vulner-

abilities in the supervision function and recommending corrective action.

While the early signs of economic activity during the last few months are very encouraging, it is important to recognize both the reality of the crisis and the remaining risks to recovery. The ruined wealth effect has been surmounted, to individuals, companies as well as the financial institutions that lent to them. Until the impact of the crisis has fully worked its way out, the most important of which is the corporate debt restructuring, the behaviour of domestic and foreign investors and financial institutions will be constrained.

In an increasingly global economy, the potential for external shocks will increase, not decline. The sharp decrease in interest rates over the last few months, together with the sizable appreciation of the exchange rate, and the positive development in price trend, are encouraging signals of a shift in market sentiments. Nevertheless, in the very short run, Indonesia needs to address the issue of corporate debt restructuring so that credit extension can resume and pressures to rupiah could be avoided. It is the only way for the economy to kick start the recovery.

It is important to understand that while bank recapitalization is necessary in the Short Run to prevent the systemic collapse of the banking system, the fact that government now owns 12 more banks that count for 75 per cent of the total liabilities of the banking system and about 90 per cent of its negative net worth, makes it very clear that this is neither desirable nor healthy for the long run development of a sound and efficient banking system.

Therefore, the overarching imperatives that would shape the next phase of the bank restructuring programme is the restructuring of the state banks and restoring the role of private sector in banking system. Hence, it is very important to watch the development of the dilution of state ownership as planned within three to five years time. The Bank Bali scandal should be taken as a lesson to learn, that in the future, transparency and good governance is a pre-requisite to a sound and fundamentally healthy banking system.

In the future, while capital inflows are certainly will be needed to fill the saving investment gap, the highly explosive nature of the balance sheet mismatch should be followed by a better approach to value at risk. That will include a good supervision of the financial system, and adherence to safe borrowing policy. While the development in financial markets goes extremely fast, it justifies to question whether a country will have the capacity to supervise the financial system. Of course, it would be ideal if there is a better management of maturities. For example, if there were contingency contracts where loans automatically are rolled over and maturities are automatically lengthened in a contingent state of illiquidity, included in the price of loan accordingly to the predictability and stability of the country. However, in spite of the available regular training, the banking supervisory capacity can easily become obsolete as market participants are always faster in creating new financial engineering instruments. This may be a good argument to allow for more foreign banks participation. Therefore, Indonesia has to decide, based on the experi-

ence on our capacity to supervise, whether to build up national domestic banks, or open up for more foreign banks. This becomes so important as, for the years to come, there will be congestion in the debt market, and countries have to compete to attract long-term financial flows. Indeed, competition for savings in the world will become fierce, and financing the Current Account deficit of the US will increase pressure on world interest rates.

In sum it makes good economic sense for Indonesia to develop and deepen its key institutions to ensure that these shocks can be absorbed through institutions cap-

able of responding quickly, justly, and in accordance with established laws and policies. At this juncture, investment in institutions could well yield higher social and economic returns than investment in physical capital. There are many areas in which institutional development is critical, but there are three key institutions need reforms: the judiciary, the civil service, and economic institutions, especially in light of the fiscal decentralization programme. It is also important to develop early warning system to detect any signal of currency crisis in the future. This policy should be supported by dissemination macroeconomic data to the public.

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